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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 37

W. G. WELBON, E. N. CLAUGHTON and
A. W. CORBETT,
Petitioners,

vs.

ATLANTIC COAST LINE RAILROAD COMPANY,
Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF
On Behalf of Petitioners

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BRIEF

On Behalf of Petitioners

I.

OPINIONS BELOW

The Court of Appeals opinions in connection with the judgment under review are reported as *In re Florida East Coast Ry Co*, 201 F2d 325 (CA 5, 1953). They are in Volume II of the record, at pages 717-733.[1]

1 This reference is to the record in No. 24 October Term, 1953. All subsequent references are to that record unless otherwise stated.

Circuit Judge Strum's District Court opinion in connection with his order disapproving the Interstate Commerce Commission's fourth plan for the reorganization of debtor under §77 of the Bankruptcy Act, which order was reversed by the judgment under review, is reported as *In re Florida East Coast Ry Co*, 103 F Supp 825 (DC Fla, 1952). It is in Volume I of the record, at pages 127-168.

Judge Strum's opinion as District Judge disapproving the first plan of reorganization is reported as *In re Florida East Coast Ry Co*, 52 F Supp 420 (DC Fla, 1943). It is in Volume VI of the record, at pages 690-697.

Circuit Judge Sibley's District Court opinion disapproving the third plan of reorganization is reported as *In re Florida East Coast Ry Co*, 81 F Supp 926 (DC Fla, 1949). It is in Volume V of the record, at pages 466-481.

The Court of Appeals opinions in connection with its judgment affirming Judge Sibley's disapproval of the third plan are reported as *Atlantic Coast Line R Co v St Joe Paper Co*, 179 F2d 538 (CA 5, 1950). They are in Exhibit B attached to the petition for certiorari herein.

The Court of Appeals opinion in a separate appeal involving the allowance of liens to the extent of money deemed to have been advanced by the bondholders does not affect the question presented here. It is reported as *In re Florida East Coast Ry Co*, 201 F2d 332 (CA 5, 1953), but is not in the record.

II.

REPORTS OF INTERSTATE COMMERCE COMMISSION

The report of April 6, 1942 approving the first plan of reorganization is reported as *Florida East Coast Ry Co Reorganization*, 252 ICC 423. It is in Volume VI of the record, at pages 528-640.

The Supplemental Report of August 10, 1942 modifying the first plan is reported as *Florida East Coast Ry Co Reorganization*, 252 ICC 731. It is in Volume VI of the record, at pages 641-689.

The Second Supplemental Report of January 8, 1945 approving the second plan is reported as *Florida East Coast Ry Co Reorganization*, 261 ICC 151. It is in Volume IV of the record, at pages 151-194.

Examiner Jewell's Proposed Third Supplemental Report is in Volume VI of the record, at pages 734-848.

The Third Supplemental Report of April 8, 1947 approving the third plan is reported as *Florida East Coast Ry Co Reorganization*, 267 ICC 295. It is in Volume IV of the record, at pages 295-391.

The Fourth Supplemental Report of March 25, 1948 adhering to the third plan is reported as *Florida East Coast Ry Co Reorganization*, 267 ICC 729. It is in Volume IV of the record, at pages 729-759.

The Fifth Supplemental Report of July 12, 1951 approving the fourth plan is reported as *Florida East Coast Ry Co Reorganization*, 282 ICC 81. It is in Volume I of the record, at pages 81-191.

The Sixth Supplemental Report of October 25, 1951 adhering to the fourth plan is reported as *Florida East Coast Ry Co Reorganization*, 282 ICC 195. It is in Volume I of the record, at pages 195-226.

III.

JURISDICTION

Jurisdiction to review the judgment of the Court of Appeals by writ of certiorari is conferred on this Court by 28 USC §1254(1).

The judgment of the Court of Appeals was rendered January 19, 1953. (II, 734) Petitioners' petition for rehearing was denied March 2, 1953.[2] Their petition for writ of certiorari was filed in this Court April 10, 1953. It was granted May 4, 1953 limited to question I presented by the petition for writ of certiorari in No. 24 October Term, 1953. (345 US 948)

IV.

QUESTION PRESENTED

The following is the question to which the Court limited review in granting certiorari (345 US 948):

> "I. It being clear that Section 77 of the Bankruptcy Act, as enacted in 1933, did not authorize the Interstate Commerce Commission to present a plan of reorganization of a railroad involving a 'forced' merger of the debtor Railway with another railroad, the question is whether amendments to the 1933 Act, made in 1935, do authorize forced mergers.

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[2] Exhibit A attached to the petition for certiorari herein.

"The Act of 1933 for railroad reorganizations in bankruptcy contained in subdivision (b) a so called consistency clause which qualified the powers of the Commission in respect of mergers, by expressly providing that a merger would have to be brought about by compliance with '*provisions*' of the Interstate Commerce Act which allowed mergers *only* if requested and agreed to by the carrier and then approved by the Commission, after notice to the Governors of the states, and after hearing communities and shippers served by the carriers. This 'consistency' provision in this legislation was repeated in subd. (e) of the 1933 Act, where it was said that transfers of property or consolidations or mergers may be made 'to the extent contemplated by the plan *consistent with the purposes* of the Interstate Commerce Act as amended'. It will be noted that the clause in (b) used the word 'provisions' and the clause in (e) used the word 'purposes'. By amendments in 1935 these two 'consistency' clauses were consolidated and transplanted from (b) and (e) to subdivision (f).

"In the 1935 Act. subd. (f), the clause allowing transfer and mergers had the qualification 'to the extent contemplated by the plan' and 'not inconsistent with the provisions and purposes of Chapter 1 of Title 49 as on August 27, 1935 or thereafter amended.'

"The narrow question is therefore whether the mere transfer of the 'consistency' clauses from subdivisions (b) and (e) to subdivision (f) altered the meaning of the clauses and gave to the Interstate Commerce Commission a power to force mergers, which was withheld from it under the Act of 1933."

V.

STATEMENT

The judgment under review was rendered by the United States Court of Appeals for the Fifth Circuit, two of five judges dissenting, in the appeal numbered and entitled on its docket 14163, *In the Matter of Florida East Coast Railway Company, Debtor—Atlantic Coast Line Railroad Company, Appellant, v St Joe Paper Company, et al, Appellees.* (II, 734)

The judgment reversed an order by Circuit Judge Strum, presiding in the United States District Court for the Southern District of Florida, Jacksonville Division.

Judge Strum's order disapproved the Interstate Commerce Commission's fourth plan for the reorganization of debtor under §77 of the Bankruptcy Act. (I, 168-170) Based on the disapproval and on a finding of "undue delay in a reasonably expeditious reorganization" of debtor, the order also dismissed the §77 proceeding and directed the return of debtor to a predecessor equity receivership, in order that the previously stayed foreclosure of the mortgage securing payment of debtors 5% bonds could be completed. (I, 169-170)

Judge Strum's grounds of disapproval were that the fourth plan, like the third, is "neither fair nor equitable" and "does not afford due recognition to the rights of the 5% bondholders, particularly the minority groups." (I, 168) He did not attempt to pass on the question of "forced merger" as such, since he believed that he was bound by "the law of the case" established in a prior appeal.[3] In that appeal disapproval of the third plan[4]

[3] *Atlantic Coast Line R Co v St Joe Paper Co*, 179 F2d 538 (CA 5, 1950)

[4] *In re Florida East Coast Ry Co*, 81 F Supp 928 (DC Fla, 1949)

was affirmed, but two of three judges who sat in the Court of Appeals disagreed with Circuit Judge Sibley's District Court decision that §77 and the Interstate Commerce Act should be construed together and, so construed, they do not authorize a plan forcing debtor into a merger, consolidation or property transfer which an overwhelming majority in amount of its bondholder-equitable owners do not consent to but oppose strongly. (81 F Supp 926)

The prevailing opinion in connection with the judgment reversing Judge Strum also followed the same law of the case. The question now presented was decided principally by reiteration of the views of the two judges in the earlier appeal. The other material parts of the opinion are largely a series of dogmatic assertions that the findings of the commission majority are supported by evidence and Judge Strum's are not, and that the commission majority was right and Judge Strum was wrong. (201 F2d 325)

The minority opinion by Judge Russell, with whom Judge Borah joined, cited Judge Sibley's District Court disapproval of the third plan and agreed with him that §77 and the Interstate Commerce Act do not authorize a plan forcing debtor into a merger, consolidation or transfer which is not consented to but is opposed by a large majority in amount of its bondholder-equitable owners. (201 F2d 325)

The question grows out of the private, non-competitive, coerced sale which would result from the enforcement against debtor's equitable owners of the so-called "forced merger" provisions of the fourth plan. They are that in the event of respondent, Atlantic Coast Line Railroad Company, accepting the commission majority's offer of sale and giving its voluntary assent:

1. All of debtor's business, assets, franchises and property shall be "vested" in Coast Line free and clear of all

of debtor's indebtedness and discharged from the lien of the 5% mortgage securing payment of $82,125,000 principal and defaulted interest coupons as of March 1, 1953.

2. The vesting shall be accomplished by merger of debtor into or its consolidation with or transfer and conveyance of its property to Coast Line.

3. The 5% bondholders shall be compelled to accept unwanted Coast Line securities having par and stated values totaling $42,500,000, together with an illusory $4,000,000 cash,[5] in extinguishment of their present equitable ownership of debtor. (282 ICC 213-226; I, 213-226)

The purport and effect of the "forced merger" provisions are that, subject to acceptance of the offer by Coast Line's equitable owners but without the consent and over the objections of debtor's equitable owners, a commission majority offered to sell debtor's property to Coast Line, [redacted] and clear of liens and debts, at a price debtor's equitable owners had no voice in fixing, which has never been determined to be the fair value of the property and is not payable in money, but represents only debtor's so-called "reorganization value" payable 91% in unacceptable Coast Line securities.

Even at this late date Coast Line is not bound. It is free to withdraw at any time. There is not and cannot be an enforceable contract between Coast Line and the commission majority.

The disapproved third plan provided for the same "forced merger," except that it would have extinguished

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[5] Judge Strum said: "*** A. C. L. puts in $4,000,000 in cash, and simultaneously receives from the estate of the debtor $4,000,000 in cash. This is a mere exchange of dollars, which benefits the present 5% bondholders not at all. The two amounts simply cancel." (103 F Supp 838)

the 5% bondholders' equitable ownership of debtor by requiring them to accept unwanted Coast Line securities having par and stated values aggregating $36,375,000, together with $4,125,000 cash. (267 ICC 747-759; IV, 747-759)

The equitable ownership of debtor by the 5% bondholders results from the fact that when the trustees holding the mortgage securing payment of their bonds brought suit to foreclose it in 1932, and had receivers appointed, debtor was and has been at all times since and is now insolvent in the bankruptcy sense of liabilities exceeding assets. It was insolvent in that sense when the 5% bondholders brought the §77 proceeding in 1941. (81 F Supp 928; 103 F Supp 828) Beginning with the Commission's first report of April 6, 1942 and continuing throughout the six supplemental reports, debtor's capital stock was found to be without value and, therefore, to represent no equity or equitable ownership, and the 5% bondholders are the senior class of creditors whose securities will not be paid in full. (VI, 588, 632, 682; 261 ICC 172; IV, 172; 267 ICC 756; IV, 756; 282 ICC 224; I, 224)

Petitioners comprise one of the minority 5% bondholder groups referred to by Judge Strum. (81 F Supp 930; 179 F2d 540) St. Joe Paper Company, a petitioner in No. 24 October Term, 1953, and affiliated interests, own a majority of the bonds. (81 F Supp 930; 179 F2d 540; 103 F Supp 842) They frequently are referred to collectively as the majority bondholder.

The "forced merger" provisions of the third and fourth plans have been consistently opposed both before the Commission and in the courts on behalf of the holders of overwhelming majorities in amount of the 5% bonds. (267 ICC 295-391; IV, 295-391; 267 ICC 729-747; IV, 729-747; 282 ICC 81-191; I, 81-191; 282 ICC 195-212; I, 195-212)

The third plan was objected to in the District Court and opposed in the Court of Appeals on behalf of the holders of more than 98% in amount. (81 F Supp 932; V, 476; 179 F2d 542; page 7 of Exhibit B attached to the petition for certiorari herein)

Objections to the fourth plan were interposed in the District Court on behalf of the holders of more than 99% in amount (103 F Supp 833; I, 138), and Coast Line's meager bondholder support disintegrated entirely before the case reached the Court of Appeals the second time. The fourth plan was not supported there, and is not supported here, by any bondholder. Coast Line was then, and is now, its only proponent.

Coast Line is one of debtor's three connecting carriers. It is not being reorganized under §77 or otherwise, is not and has never been affiliated with debtor in any way, and has never controlled or been controlled by debtor, nor has either ever had any proprietary interest in the other. The two railroads have never been commonly owned or controlled. There has never been any interlocking, overlapping or integration of their financial structures. They have always been completely independent of each other, their only relationships having been that of connecting carriers and joint owners of a steamship line from Miami to Cuba. (267 ICC 295-391; IV, 295-391; 267 ICC 729-747; IV 729-747; 81 F Supp 926; V, 466-481; 179 F2d 538; pages 1-22 of Exhibit B attached to the petition for certiorari herein; 282 ICC 81-191; I, 81-191; 282 ICC 195-212; I, 195-212; 103 F Supp 825; I, 127-168; 201 F2d 325; II, 717-733)

Debtor's capital structure is simple and uncomplicated. It is (103 F Supp 828):

First Mortgage 4½% Bonds due January 1, 1959 (Originally $12,000,000)	$ 8,189,000
First and Refunding Mortgage 5% Bonds due September 1, 1974	45,000,000
Capital Stock	37,500,000
Total	$90,689,000

During the pendency of the reorganization proceeding debtor's trustees have purchased from earnings and now hold $3,811,000 of the $12,000,000 first mortgage bonds. They and their predecessor receivers have paid from earnings all interest due on the bonds of that issue. The issue is not and has never been in default. They also have on hand accumulated earnings more than sufficient to retire the principal. (103 F Supp 828)

When Judge Strum disapproved the fourth plan they had paid from earnings $7,875,000 defaulted interest on the 5% bonds. (103 F Supp 828) They have since paid from earnings $4,500,000 additional defaulted interest. As of March 1, 1953 the interest coupons in default amounted to $37,125,000.

Debtor is the only double track railroad in Florida. It owns and operates 366 miles of modern rock ballasted main line double track on the east coast of Florida from Jacksonville, the second largest city in the state, to Miami, the largest. It is the most direct railroad connection between those cities. It also owns and operates single track branch lines which increase its total operated track to 571 miles. The branch lines extend to the truck-growing areas around Lake Okeechobee and those south of Miami. New Industries are constantly being located along its lines, one of

which alone will produce to debtor an annual revenue of $700,000. (103 F Supp, 842-843)

From Jacksonville south to the Palm Beaches, a distance of 299 miles, debtor has no rail competition and is the only rail carrier serving St. Augustine, Daytona Beach, New Smyrna Beach, Titusville, Cocoa, Melbourne, Vero Beach, Fort Pierce, Stuart and smaller communities. From the Palm Beaches south to Miami it serves Lake Worth, Boynton Beach, Delray Beach, Boca Raton, Deerfield Beach, Pompano Beach, Fort Lauderdale, Fort Everglades, Dania, Hollywood and smaller communities, in competition with Seaboard Airline Railway. (103 F Supp 843)

Debtor's lines are fully protected by the most modern electrically operated safety system. They have reeently been rerailed with new 112 and 115 pound steel rails at a cost of approximately $9,000,000, all paid out of earnings. Its rolling stock, purchased mainly from earnings, consists largely of Diesel locomotives, the latest and most modern streamlined passenger equipment and adequate modern freight equipment, with which it provides fast freight and local service and with its connecting carriers furnishes daily passenger service in high speed trains from New York, Chicago, Detroit and other points, via Jacksonville, to Miami and intermediate points. (103 F Supp. 843)

Coast Line, Seaboard and Southern Railway are debtor's connecting carriers at Jacksonville. They now compete for debtor's interchange business through the Jacksonville "open gateway." Debtor has no other connecting carrier. (103 F Supp 845)

Seaboard and Southern are petitioners in No. 24 October Term, 1953. Before the Commission and in the lower courts they vigorously objected to the proposed merger, consolidation or transfer. (267 ICC 336-339; IV, 336-339; 81

F Supp 927; 179 F2d 539; 282 ICC 140-142; I, 140-142; 103 F Supp 827; 201 F2d 325)

Coast Line has a double track main line from Richmond to Jacksonville, and main lines from Jacksonville to Tampa, Birmingham and Atlanta, but has no line from Jacksonville to Miami. (179 F2d 541; 103 F Supp 844) Coast Line's basic purpose in submitting to the Commission offers to purchase debtor's property, and the basic purpose of the commission majorities in making counter-offers of sale, was to enable Coast Line to acquire at a bargain debtor's double track main line from Jacksonville to Miami. (81 F Supp 934; 179 F2d 542; 103 F Supp 844)

Coast Line's President made the following statement to its Board of Directors:

> "**** the rails of the Florida East Coast Railway represent a logical extension of this Company's lines into the lucrative East Coast section of Florida, not now directly served by this Company, and that he has for a number of years considered it was desirable that this Company should acquire that property or control thereof and operate same as a part of this Company's system *** the property operated as part of this Company, with consequent operating savings, should produce average annual net earnings available for fixed charges of about $1,700,000, which would be sufficient to meet reasonable fixed and contingent charges and *leave some residue of profit for this Company.* *** the advantages of being an 'originating' and 'terminating' line in Florida East Coast territory, which is perhaps the most highly developed section of the State of Florida, should produce for this Company *added earnings* on additional traffic which would be transported by this Company beyond the line of the present Florida East Coast Railway, that is, north

of Jacksonville, although the amount of such added earnings cannot be properly evaluated." (Emphasis supplied—St Joe Paper Co Exhibit X)

The Board immediately adopted a resolution authorizing the Chairman or the President to file such applications or petitions to the Commission or the court, and take such other and further action in connection with the reorganization of debtor, as might be necessary to effect the purchase by Coast Line of "Common Stock of the reorganized company."

During the pendency of the reorganization proceeding Coast Line purchased unsecured claims against debtor aggregating $1,900,000 which the Commission had found to be without value. It paid $5,000 for the claims and agreed with the former owners to pay an additional 50% of whatever might be realized on them, less expenses. Until it bought the unsecured claims, Coast Line never had any financial interest in debtor, and was not even a creditor. (VI, 920-921; IV, 144-146)

Coast Line's initial appearance in the proceeding came after Judge Strum had disapproved the Commission's first plan[6] and hearings before the Commission on a second plan had been closed. The appearance took the form of a petition to have the proceeding reopened for the submission of a plan under which Coast Line would acquire control of the reorganized debtor by a forced sale to Coast Line of 60% of the new common stock. (261 ICC 187-193; IV, 187-193)

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6 The plan provided that the 4½% first mortgage bondholders should receive new first mortgage bonds equal in amount and seniority to the bonds then held, and the 5% bondholders should receive, for each $1,000 bond, $100 of new general mortgage bonds and 10 shares of no par value stock. (252 ICC 423; VI, 528; 252 ICC 731; VI, 641) It was disapproved solely on the ground that it should have allocated for reorganization purposes, instead of leaving as a floating surplus, accumulated earnings amounting to approximately $17,000,000. (52 F Supp 420; VI, 690-697)

The Commission unanimously rejected this proposal[7] and approved a second plan providing for the 4½% first mortgage bonds to be paid in full from accumulated earnings, the setting aside of $8,700,000 from accumulated earnings as reserves for betterments and improvements and cash requirements upon reorganization, and the receipt by the 5% bondholders, for each $1,000 bond, of $450 new first mortgage income bonds and 4½ shares of new common stock. (261 ICC 170-187; IV, 170-187)

On petitions for modification the Commission reopened the proceeding and Coast Line proposed the "forced merger." (267 ICC 295-298; IV, 295-298) The proposal was a unilateral offer by Coast Line to purchase debtor's property. The offer was submitted to the Commission for acceptance. It was not made to the debtor, its trustees or equitable owners, and did not have their concurrence or consent. It was not binding on Coast Line. (267 ICC 300; IV, 300)

After lengthy hearings, the Examiner's full and carefully considered report recommended strongly that the second plan be modified in relatively minor respects and otherwise be adhered to. (VI, 734-848)

By a five to four vote,[8] the Commission overruled the Examiner and approved Coast Line's "forced merger"

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7 For the reasons, among others, that the securities proposed, taken at par, would fall far short of satisfying the amount of the claim of the 5% bondholders and if, in their view, the prospects of future earnings or the control value were such that the stock might later have a market value in excess of par and they desired to hold it to realize the higher price, they should be at liberty to do so, as they would not be reimbursed in full on their claim by accepting $100 per share for stock representing a part of their share of debtor's estate; the majority bondholder would vote to reject the proposal; the §77 power to order a judicial sale of the property of debtor for the benefit of creditors did not confer power "to sell the interests of one or all the creditors to another creditor or to an outsider for the benefit of the purchaser"; and the proposal was prima facie impracticable. (261 ICC 187-193; IV, 187-193)

8 In Commissioner Mahaffie's first dissent (267 ICC 390; IV, 390), in which four other Commissioners joined, some initially, others later (267 ICC 747; IV, 747), he said: "Aside from what seems to me a fatal legal

proposal, with modifications, as the Commission's third plan. (267 ICC 390-391; IV, 390-391) By this approval the majority made a counter-offer to sell debtor's property to Coast Line at a price slightly higher than the one Coast Line had offered to pay. Coast Line could not accept the counter-offer without first amending its charter to authorize the issuance of the class of preferred stock provided for.[9] Coast Line's stockholders avidly adopted a resolution accepting the counter-offer and assenting to the acquisition of debtor's property.[10]

The report making the counter-offer refused to permit a judicial sale of the property. The reason given was that it would defeat the proposed transfer, "since Coast Line obviously could not compete successfully in bidding with the debtor's first and refunding bondholders." (267 ICC 307; IV, 307)

Upon reconsideration by the full Commission the counter-offer was adhered to by a six to five vote. (267 ICC 729-747; IV, 729-747) The report adhering to it stated that the offering price did not "represent worth of the property such as would be determined by an inventory of the physical assets," nor "physical value," nor "market

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defect in the report, I think it wrong on the merits. *** I would approve a plan which, in its main features, is substantially as proposed by the examiner. This would permit the property to be reorganized. The result of the present report, in my judgment, is more likely to be prolonged litigation." (267 ICC 391; IV, 391)

9 "RESOLVED, that in order to effect the acquisition of the properties of Florida East Coast Railway Company and to issue the class of preferred stock specified by the Interstate Commerce Commission in its Report and Order dated March 25th, 1948, this Board of Directors of this Company now recommends to the stockholders that the Charter of this Company as now existing be amended ***." (III. St Joe Paper Co Exhibit X, resolution adopted by Coast Line's Board of Directors)

10 "RESOLVED, that the Stockholders of Atlantic Coast Line Railroad Company in meeting assembled do hereby accept the Plan of reorganization of Florida East Coast Railway Company, as approved by the Interstate Commerce Commission in its Reports and Orders, dated April 8th, 1947, and March 25th, 1948, in the pending Florida East Coast Railway Company reorganization proceeding, and hereby assent to the acquisition of the properties of that Company by Atlantic Coast Line Railroad Company as provided in said Plan ***." (III. St Joe Paper Co Exhibit X).

value," but represented only debtor's "Value for reorganization purposes" payable in Coast Line securities. (267 ICC 736; IV, 736)

The plan was disapproved by Circuit Judge Sibley presiding in the District Court, (81 F Supp 926; V, 466). His grounds were that §77 and the Interstate Commerce Act, construed together, did not authorize a plan forcing debtor into a merger, consolidation or transfer to which the 5% "bondholders by an overwhelming majority do not consent" (81 F Supp 932; V, 476), but if it did, and was within constitutional bankruptcy power, the plan was not fair and equitable and did not afford due recognition to the rights of the bondholders.

The Court of Appeals affirmed, one of three judges dissenting. (179 F2d 538; pages 1-22 of Exhibit B attached to the petition for certiorari herein)

This Court denied Coast Line's petition for certiorari. (339 US 929) However, two judges in the Court of Appeals concluded that Judge Sibley was wrong on the question of "forced merger." Chief Judge Hutcheson said, and the effect of Judge Holmes' dissenting opinion was to agree, "that a plan providing for what the trial judge broadly called a 'forced merger', that is, a merger over the objection of the debtor and all its creditors, might be lawfully certified to the court and lawfully approved and confirmed by it." (179 F2d 544)

So far as can be ascertained from their respective opinions, neither appellate judge gave any consideration to the effect of the "consistency" clause in §77(f), conferring on the Commission limited power, "upon confirmation of a plan," to "grant authority for the *** transfer of any property, sale, consolidation or merger of the debtor's property *** to the extent contemplated by the plan *and not inconsistent with the provisions and pur-*

poses of the Interstate Commerce Act as now or hereafter amended." (Emphasis supplied)

Judge Russell concurred in Chief Judge Hutcheson's opinion only to the extent that it affirmed Judge Sibley's order, but said he was in "complete accord" with Judge Sibley's conclusions and could not accept contrary views expressed by Chief Judge Hutcheson. (179 F2d 545) Thus he agreed with Judge Sibley's decision that §77 and the Interstate Commerce Act do not authorize a plan forcing debtor into a merger, consolidation or transfer which an overwhelming majority in amount of its bondholder-equitable owners do not consent to but oppose.

The views of Judges Hutcheson and Holmes on the question of "forced merger" have been regarded by the Commission and the courts as the law of the case in all subsequent proceedings.

Coast Line proposed another "forced merger." (282 ICC 87; I, 87) This proposal, too, was a unilateral offer to purchase debtor's property at a price claimed to be better than the one fixed by the commission majority in the disapproved third plan. The new offer, like the first, was submitted to the Commission for acceptance. It was not made to the debtor, its trustees or equitable owners. It did not have their concurrence or consent. Like the first offer, it was not binding on Coast Line.

With modifications, Coast Line's new "forced merger" proposal was approved by a seven to three vote as the Commission's fourth plan. (282 ICC 81-191; I, 81-191) By this approval the commission majority made another counter-offer to sell debtor's property to Coast Line, asserting that the new price was better than the one fixed in the earlier counter-offer.[11] Coast Line's stockholders adopted

[11] Judge Strum found: "*** the bondholders are receiving, for the property itself, $1,340,000 less under the fourth plan than under the third." (103 F Supp 840)

a resolution accepting the new offer and assenting to the acquisition of debtor's property.[12]

Unlike the report making the earlier counter-offer, the report making the new one says nothing about a judicial sale, but it does not provide for one. (282 ICC 81; I, 81; 282 ICC 213; I, 213) It does say that the new offering price represents "the value of the debtor's property in terms of Coast Line securities, including one-half of the prospective savings." (282 ICC 160; I, 160)

Petitions for modification submitted by these petitioners and others were denied by a seven to three vote. (282 ICC 195-212; I, 195-212)

Judge Strum disapproved the plan as unfair, inequitable, and not a due recognition of the rights of the 5% bondholders. (I, 168-170)

Much of the prevailing opinion reversing Judge Strum is devoted to an exposition of the areas of agreement and disagreement between Judges Hutcheson and Holmes in the prior appeal. The opinion then says: "Turning, for the correct answer to this question, to the record as it now stands before us, we are not in any doubt that, under the plain terms of subsection (b)(5) of Sec. 77 of the Act, 11 U.S.C.A.§205, which provides that the plan 'may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations *** ' the commission was precisely authorized to formulate and recommend a plan providing, as the fourth plan does,

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12 "RESOLVED, that the Stockholders of Atlantic Coast Line Railroad Company in meeting assembled do hereby accept the Plan of Reorganization of Florida East Coast Railway Company, as approved by the Interstate Commerce Commission in its Reports and Orders, dated July 12th, 1951, and October 25th, 1951, in the pending Florida East Coast Railway Company re-organization proceeding, and hereby assent to the acquisition of the properties of that Company by Atlantic Coast Line Railroad Company as provided in said Plan ***."

for the merger of East Coast and Coast Line." (201 F2d 329)

This opinion, too, fails to disclose that any consideration was given to the limitation of power imposed on the Commission by the "consistency" clause in §77(f).

Judge Borah joined in Judge Russell's dissenting opinion. It points out that "The bald proposition established by the majority opinion is that the court's power in bankruptcy authorizes the taking, against the wishes of the overwhelming majority of the refunding bondholders, of their existing rights, requiring acceptance by them of an entirely different and unrelated security which they do not desire." It says that "This holding poses a serious constitutional question as to whether the court's power in bankruptcy could thus be extended to force a merger consistent with the Fifth Amendment." (201 F2d 331)

The dissent goes on to say: "*** I do not reach the constitutional question because here it is clear from the history of the legislation of Section 77, that the Commission has undertaken to exercise a power which the Congress never intended to confer on the Commission. This was well pointed out by Judge Sibley in his decision while sitting as District Judge in a former proceeding in this matter. *** This view was expressly approved by the writer in his special concurrence upon the former appeal of this case. *** It is reaffirmed today." (201 F2d 331-332)

Petitioners submitted the only petition for rehearing. It was denied. Judges Russell and Borah dissented. (Exhibit A attached to the petition for certiorari herein)

A truly remarkable aspect of the case is that every presiding officer who heard evidence disapproved the pro-

posed forced merger, and all decisions approving it were by commissioners or judges who had neither seen nor heard any witness and were not as well qualified to evaluate the evidence.

Examiner Jewell heard evidence in Washington, D. C., November 6-9, 1945 and in West Palm Beach, Florida, November 13-30, 1945. (VI, 735-736) He recommended that the Commission disapprove the proposed forced merger. (VI, 797-798) Judge Sibley heard evidence in Jacksonville, Florida, January 10-13, 1949. (IV, 118; V, 461) He disapproved the third plan. (81 F Supp 926) Judge Strum heard evidence in Jacksonville, Florida, February 4-7, 1952. (II, 247, 659) He disapproved the fourth plan. (103 F Supp 825)

No evidence was heard by the five Commissioners who overruled Examiner Jewell and made the first counter-offer of sale (267 ICC 297; IV, 297), nor was any heard by the six Commissioners who adhered to the report overruling him (267 ICC 729; IV, 729), nor by the seven Commissioners who made the second counter-offer of sale (282 ICC 81; I, 81), nor by any judge who sat in the Court of Appeals.

VI.

SPECIFICATION OF ERRORS

The Court of Appeals erred in the following respects:

1. In deciding that §77 of the Bankruptcy Act authorizes the so-called "forced merger" plan of reorganization.

2. In deciding that §77(b) of the Bankruptcy Act confers on the Interstate Commerce Commission power to approve and certify a plan of reorganization providing, without the assent and over the objections of an overwhelming majority in amount of debtor's equitable owners, for a merger, consolidation or transfer resulting from the Commission's having entertained and considered respondent's unilateral offer to purchase debtor's property, and the acceptance by respondent of a commission majority counter-offer to sell it.

3. In reversing Judge Strum's order disapproving the so-called "forced merger" fourth plan of reorganization.

4. In directing Judge Strum to approve the so-called "forced merger" fourth plan of reorganization.

VII.

SUMMARY OF ARGUMENT

1. The Commission did not have power to approve or certify the so-called "forced merger" plan of reorganization. The consistency clause in §77(f) of the Bankruptcy Act requires the construction in pari materia of the merger, consolidation and transfer provisions of §5 of the Interstate Commerce Act and §77(b) of the Bankruptcy Act. Review of the integrated provisions of §77 and §5 establishes that Congress intended and required that all mergers, consolidations and transfers should be carrier-initiated and voluntary.

The combined consistency clause in §77(f) of the 1935 Act, like its two predecessors in §77(b) and (e) of the 1933 Act, requires consistency with both the "provisions and purposes" of the Interstate Commerce Act. The fact that the combined clause is framed in the form of a limitation on the powers exercisable by the Commission after confirmation does not govern its application. The Commission must determine that a merger, consolidation or transfer will be "consistent" before it can approve or certify a plan, otherwise the certified plan will be lacking in permissible means of execution.

2. The 5% bondholders are debtor's equitable owners and in that capacity are entitled to vote under §5(11) of the Interstate Commerce Act on the question of corporate assent by debtor to the merger, consolidation or transfer. If debtor's capital stock represented value and equitable ownership, the stockholders would be entitled to vote under §5(11) on the question of corporate assent. The 5% bondholders are in fact the equitable owners. They stepped into the shoes of the stockholders, and in those shoes succeeded to the right to vote. To say that the right is con-

trolled by the technicality of stock-ownership, as against bond-ownership, rather than by equitable ownership would sacrifice substance to form:

3. The "cram-down" provision in §77(e) of the Bankruptcy Act conferred no power on the Commission. It gave the court, but not the Commission, a new power.

4. The court's "cram-down" power does not authorize confirmation of the so-called "forced merger" plan of reorganization. It does not apply to the first vote—the group vote of equitable owners on the question of corporate assent to the merger, consolidation or transfer, to be taken under §5(11) of the Interstate Commerce Act. The power applies solely to the second vote in connection with a plan providing for a merger, consolidation or transfer. This is the individual vote of each affected creditor or equitable owner, to be taken under §77(e) of the Bankruptcy Act, on the question of acceptance or rejection of a plan approved by Commission and court. The factors and considerations involved in this vote have long been within the equity and bankruptcy jurisdiction of courts—fair and equitable treatment, due recognition of rights, unfair discrimination, conformity to requirements of law of land, and reasonable justification for rejective action.

The cram-down provision does not confer power on the court to determine or decide what is best for owners in regard to keeping or selling property they have chosen and lawfully own, it being a fundamental concept of our system of government that what a man chooses to own, if lawful, cannot be taken away from him in consideration of something that a court thinks is as good or better, except under the power of eminent domain.

The purpose of the cram-down provision is to prevent dissident minorities, in the sense of minority classes of inferior claims in a complicated financial structure, a

situation which does not exist here, from blocking confirmation of a plan approved by Commission and court—to obviate the exacting of inequitable adjustments by obstructive minorities as the price of their consents.

Because Congress intended constitutional application of the cram-down provision, it should not be given the unconstitutional application proposed by the commission and court of appeals majorities.

5. The 1935 amendments to §77 do not authorize the "forced merger," because the inclusion in §77(e) of the *Boyd* case "fair and equitable" standard requires the retention of creditors' property rights as in equity receiverships and precludes their divestment by "forced merger."

VIII.

ARGUMENT

1. The Commission Did Not Have Power to Approve or Certify the So-Called "Forced Merger" Plan of Reorganization.

The provisions of §77 of the Bankruptcy Act[13] expressly integrate §77 with the Interstate Commerce Act, thus requiring that they be construed in pari materia to ascertain and give effect to the intent of Congress.

The consistency clause in §77(f) requires that a merger, consolidation or property transfer provided for in a plan of reorganization shall be consistent with the "provisions and purposes" of the Interstate Commerce Act. Thus, it requires the construction in pari materia of the merger, consolidation and transfer provisions of §5 of the Interstate Commerce Act and §77(b) of the Bankruptcy Act.

So construed, the manifest intent and explicit provisions are that the consistency clause limits the Commission's §77(b) merger, consolidation and transfer powers to those conferred by the Interstate Commerce Act, and precludes the approval or certification by the Commission of a plan of reorganization providing for a merger, consolidation or transfer which has not been consented to by the requisite majority of a debtor's equitable owners.

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13 The material parts of statutes referred to are set out in appendices.

Appendix A sets out in parallel columns the pertinent parts of §77 of the Bankruptcy Act, as enacted originally in 1933 and as revised in 1935, in order that the changes in their provisions may be noted.

Appendix B sets out the pertinent parts of §5 of the Interstate Commerce Act, as enacted by the Transportation Act of 1920 and codified in 49 USCA §5.

Appendix C sets out the pertinent parts of §5 of the Interstate Commerce Act, as amended by the Transportation Act of 1940 and codified in 49 USCA §5, pocket part supplement.

The integration of the two Acts is demonstrated in *Thompson v Texas Mexican R Co*, 328 US 134, 144 (1946), which says:

> "The commission has further functions to perform apart from determining under §77 whether it would be consistent with the reorganization requirements of the debtor to terminate the trackage agreement.
>
> "By §1(18) of the Interstate Commerce Act, 49 USCA §1(18) 10A FCA title 49, §1(18), it is provided that 'no carrier by railroad subject to this chapter shall abandon all or any portion of a line of railroad, or the operation thereof, unless and until there shall first have been obtained from the commission a certificate that the present or future public convenience and necessity permit of such abandonment.' *Carriers being reorganized under §77 of the Bankruptcy Act are not exempt from that provision.*" (Emphasis supplied)

It would be strange indeed if Congress had intended that a debtor in a §77 reorganization proceeding could not be authorized to abandon a trackage agreement except in compliance with the Interstate Commerce Act, but could be deprived of all property by forced merger, consolidation or transfer without regard to its provisions.

The integration of the two Acts was not noticed or discussed in any of the prevailing opinions in the Court of Appeals. The consistency clause in §77(f) was not mentioned or referred to. Nothing was said regarding its effect. So far as those opinions are concerned it does not exist.

It was discussed by the commission majorities. In the third supplemental report the majority said (267 ICC 308; IV, 308):

"The Coast Line plan, by which control would be transferred to that carrier, is in effect a request or application to us by one carrier for authority to acquire control of another and, in conformity with the provisions of subsection (f) of section 77 of the Bankruptcy Act that the transfer of the properties of a debtor be not inconsistent with the provisions and purposes of the Interstate Commerce Act, the record should contain the information required in a proceeding under section 5(2) of the Interstate Commerce Act."

In contrast, the majority said in the fourth supplemental report that the consistency clause in §77(f) "is not a limitation on the plan which we are authorized to approve under subsection (b)." (267 ICC 731)

The effect of that statement, as applied, was to assert that Coast Line could submit to the Commission a unilateral offer to acquire debtor's property, and the Commission could accept it or make a counter-offer for acceptance or rejection by Coast Line, all without the concurrence or consent of the debtor, its trustees or equitable owners.

To the contrary, review of the integrated provisions of the controlling statutes establishes that Congress intended and required that all mergers, consolidations and transfers should be carrier-initiated and voluntary. The requirements are that every merger, consolidation or transfer, whether involving solvent railroads or debtor railroads in §77 proceedings, or both, must be the voluntary result of arm's length bargaining between or among them, and be assented to by the requisite majorities of the equitable owners of each railroad involved. Until 1940 it also was required that every merger, consolidation or transfer be in harmony with and in furtherance of the nation-wide

plan of consolidations adopted in compliance with the Transportation Act of 1920. The Commission's statutory power is that, with the assent of each railroad involved, and upon proper application, notice and hearing, it can approve and authorize a voluntary merger, consolidation or transfer, but it has never been given the power to coerce one.

As enacted by the Transportation Act of 1920,[14] §5 of the Interstate Commerce Act directed the Commission to "prepare and adopt" a nation-wide plan for the consolidation of railroads into "a limited number of systems."[15] It gave the Commission power to approve and authorize consolidations "if all the carriers involved assent thereto,"[16] and if "in harmony with and in furtherance of" the nation-wide plan of consolidations.[17] It did not confer power to compel them.[18] The purpose of these provisions was to permit and encourage railroad-initiated voluntary consolidations assented to by "all the carriers involved," conforming to the nation-wide plan.[19]

In the nation-wide plan adopted in 1929[20] debtor was allocated to the Southern Railway System. (267 ICC 343; IV, 343) Thus, even a carrier-initiated voluntary agreement, assented to by both railroads, for the merger or consolidation of debtor with or the transfer of its property to Coast Line would have violated the nation-wide plan when §77 of the Bankruptcy Act was enacted in 1933, and when it was revised in 1935, and until the Transportation

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14 Act of February 28, 1920, 41 Stat 456, c 91, 49 USCA §5

15 §407(4), 49 USCA §5(4)

16 §407(6)(c), 49 USCA §5(6)(c)

17 §407(6)(a), 49 USCA §5(6)(a)

18 *Schwabacher v United States*, 334 US 182 (1948)

19 Case cited in footnote 18

20 Consolidation of Railroads, 159 ICC 522

Act of 1940[21] released the Commission from adherence to the nation-wide plan.

When §77 was enacted in 1933,[22] and when it was revised in 1935,[23] §5 of the Interstate Commerce Act was not changed. As enacted originally, §77 required that any plan of reorganization recommended by the Commission to the interested parties (§77(d)) should provide adequate means for its execution. (§77(b)) The means could include a merger, consolidation or transfer "so far" as would be "consistent with the provisions of §§ 1 and 5 of the Interstate Commerce Act as amended." (§77(b))

This could mean only a merger, consolidation or transfer to which "all the carriers involved assent" and in "harmony with and in furtherance of" the nation-wide plan. It limited the merger, consolidation and transfer powers of the Commission to those conferred by §5 of the Interstate Commerce Act. It limited the Commission to the previously conferred power of approval and authorization, and did not confer a new power to compel.

That this was the meaning is borne out by the subsequent provision that, following acceptance of a plan by the affected creditors and stockholders, the Commission could approve it and grant authority to effectuate any merger, consolidation or transfer provided for "consistent with the *purposes* of the Interstate Commerce Act as amended" (§77(e)—emphasis supplied), one of which was to encourage the railroad consolidations authorized by §5.

When §77 was revised in 1935, §5 of the Interstate Commerce Act was not changed. It continued to provide that

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21 Act of September 18, 1940, 54 Stat 898, c 722, 49 USCA §5(2)

22 Act of March 3, 1933, 47 Stat 1474, c 204

23 Act of August 27, 1935, 49 Stat 911, c 774

the Commission could approve and authorize a consolidation only "if all the carriers involved assent thereto" and if in conformity with the nation-wide plan.

The two consistency clauses in §77(b) and (e) of the 1933 Act were combined and transferred to §77(f) in the 1935 revision. The combined clause is that "Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the * * * transfer of any property, sale, consolidation or merger of the debtor's property *** to the extent contemplated by the plan and *not inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended.*" (Emphasis supplied)

The 1935 revision requires that a commission approved plan provide adequate means for its execution. (§77(b)) The means may include a merger, consolidation or transfer (§77(b)), but the Commission cannot grant authority to effectuate a merger, consolidation or transfer "inconsistent with the provisions and purposes of the Interstate Commerce Act." (§77(f)) Necessarily, a merger, consolidation or transfer which the Commission cannot grant authority to effectuate cannot be the means for the execution of a plan.

Section 5 of the Interstate Commerce Act was amended by the Transportation Act of 1940,[24] but the combined consistency clause in §77(f) of the Bankruptcy Act was not changed. It continues to require that a merger, consolidation or transfer provided for in a plan of reorganization shall not be "inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended."

"The Transportation Act of 1940 relieved the Commission of formulating a nation-wide plan of consolidations.

24 Act of September 18, 1940, 54 Stat 898, c 722, 49 USCA §5

Instead, it authorized approval by the Commission of carrier-initiated, voluntary plans of merger or consolidation * * * ." [25]

Under §5(2)(a) of the Interstate Commerce Act, as amended by the Transportation Act of 1940, the Commission may approve and authorize a voluntary merger or consolidation of two or more railroads, or one railroad's voluntary sale of its property to another. Approval of a voluntary merger, consolidation or transfer "within the scope of the Act is dependent upon three, and upon only three, considerations: First, a finding that it 'will be consistent with the public interest.' (§5(2)(b)) Second, a finding that, subject to any modification made by the Commission, it is 'just and reasonable.' (§5(2)(b)) Third, assent of a 'majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the shares entitled to vote.' (§5(11))" [26]

Reading all of these provisions together, they make it crystal clear that the Commission does not have the power to approve or certify a plan of reorganization providing, without the consent and over the objection of a debtor's equitable owners, for a merger, consolidation or transfer resulting from the Commission's having entertained and considered another railroad's unilateral offer to acquire the debtor's property, and the acceptance by the other railroad of a commission majority counter-offer to dispose of it.

The statutory provisions limit the Commission's merger, consolidation and transfer powers to approval and authorization of voluntary mergers, consolidations and transfers resulting from arm's length bargaining between the

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25 *Schwabacher v United States*, 334 US 182, 193 (1948)

26 *Schwabacher v United States*, 334 US 182, 194 (1948)

railroads involved. This was provided not only because it is the historic American approach to the process of purchase and sale, but also because it is the only means by which the equitable owers of each railroad can be reasonably assured that they will not be deprived, even by honest mistake, of any value to which they may be entitled.

It is the only method by which the equitable owners of each railroad can claim and enforce their right to be paid the values which they believe to be inherent in their property. It is the only way in which equitable owners, as investors, can preserve intact their right to be paid or have the benefit of future earnings, and to determine when, how and for what consideration they will dispose of that right.

There was no arm's length bargaining here. The sale price fixed by the commission majority in its last counter-offer does not represent a price negotiated by owners willing but not compelled to sell and a buyer desirous but not compelled to purchase.

Debtor's equitable owners had no voice in fixing the price for which the commission majority says their property must be sold. All they have been able to do is to clamor that the Commission has no power to sell it, but nevertheless is offering it for sale at an unconscionably low price. And if the Court of Appeals majority is right, there can be no judicial review of the question whether the commission majority's offering price is unconscionably low.

Inherent in all that was done is the undeniable fact that the commission majority could not adopt an owner's bargaining approach, nor could it exercise an owner's bargaining latitude. An owner can set his price and lower or

increase it as he sees fit, or as may become necessary or advisable because of his necessities, financial difficulties, prosperity or other changing circumstances. He can make an offer and tell the prospective buyer to "take it or leave it." Normally he is not under compulsion to fix a price which he believes will prove attractive to a prospective purchaser.

The commission majority was under that compulsion. It had to set a price which it thought would prove attractive to Coast Line. To set one which it thought would not prove attractive—one which it thought Coast Line would not accept—would have been futile. To be certain of not setting a price higher than Coast Line would be willing to pay, the majority had to subordinate the rights of debtor's equitable owners to the primary objective of making it possible for Coast Line to purchase debtor's double track main line from Jacksonville to Miami. All other things—rights, values, equities, purchase price and terms of payment—had to be secondary and subordinate to that objective.

That the commission majority, in order to be assured of effecting a sale to Coast Line, was compelled to and did sacrifice the rights, values and equities of debtor's equitable owners to the fixing of a price and terms of payment which it thought would prove attractive to Coast Line, is demonstrated by the developments in this case.

Coast Line first made the Commission an offer to buy 60% of the reorganized debtor's common stock. (261 ICC 187; IV, 187) The Commission unanimously rejected the offer. (261 ICC 190-193; IV, 190-193)

Coast Line then made the Commission an offer to purchase debtor's property. (267 ICC 296; IV, 296) The Commission found expressly that the offer "is inequitable in that it does not provide for full satisfaction of the value

of the claims of the debtor's creditors." (267 ICC 389, par 15; IV, 389, par 15)

A commission majority made a counter-offer. (267 ICC 372; IV, 372) Coast Line accepted. (III, St Joe Paper Co Exhibit X)

Presumably the majority thought its counter-offer was equitable, but Judge Sibley found that it was not fair and equitable and did not afford due recognization to the rights of the 5% bondholders. (81 F Supp 926) The Court of Appeals affirmed. (179 F2d 538) This Court denied certiorari. (339 US 929)

Judge Sibley said: "The very aggressiveness of the Coast Line in proposing and defending this plan indicates that the Coast Line thinks it is getting a bargain; that what it gets is not the mere equivalent of what it pays, but much more." (81 F Supp 934) Chief Judge Hutcheson added: "The case we have here is that of one railroad company coveting, and pressing to possess, a competing debtor railroad company, against the wishes of 98 percent of the equitable owners of the debtor ***." (179 F2d 542)

Following the final disapproval of the third plan, Coast Line made another offer to the Commission. (282 ICC 87; I, 87) The Commission found that the new offer "would not fully compensate the debtor's creditors for surrendering their property rights." (282 ICC 163; I, 163)

A commission majority made another counter-offer. (282 ICC 181; I, 181) Coast Line accepted. (III, ACL Exhibit 10)

Presumably the majority thought the second counter-offer was equitable, but Judge Strum found that, like the first counter-offer, it is "neither fair nor equitable" and "does not afford due recognition to the rights of the 5%

bondholders, particularly the minority groups." (I, 168-170) Three of the five judges who sat in the Court of Appeals differed with him, and thought the commission majority had set a sufficient price. (201 F2d 325)

The controlling statutes do not contemplate any such dickerings between Coast Line and the commission majorities, with debtor's equitable owners excluded from any voice in fixing the price at which the commission majority offered to sell their property.

Judge Sibley's views, in which Judges Russell and Borah emphatically concurred, are cogent and compelling. They were that the Interstate Commerce Act is to be construed with §77 to ascertain the intent of Congress and, so construed, they authorize the Commission to approve bilateral agreements for mergers or consolidations of railroads or transfers of their property, but do not confer authority for the Commission to enter into negotiations with Coast Line for the sale of debtor's property, Judge Sibley said (81 F Supp 932-933):

> "It is very earnestly argued that Subsection b which gives the specifications for a plan, in saying it 'may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation,' etc., does not mean a forced merger, which the Interstate Commerce Act, 49 U. S. C. A. §1 et seq., has never permitted the Commission to compel, though Congress has often considered the matter. The history of the legislation in adopting Section 77 in 1933, is pointed to as showing that Congress was then concerned that no such thing was to be done under Section 77; and so again in 1935 when the section was revised; and that the reference to the Interstate Commerce Act in Subsection f which the Commission

thinks applies only to its actions after confirmation of a plan, was intended to apply throughout and became accidentally misplaced in redrafting the Act. Without reciting the history, I think this contention is true. *** this question *** relates to the extent of the power granted by Congress to its own agent. And the Interstate Commerce Act can be construed with Section 77 to ascertain what Congress really meant by a railroad 'merger or consolidation', and whether it means one consented to by both parties to it. No one would contend that the Coast Line could be forced. But the Commission argues that this debtor has also consented, because its stockholders have not appeared to object. I think that does not follow. It is expressly found that the debtor's insolvency is such that the stockholders are not interested parties. The debtor, its property and affairs now belong in equity to the creditors, and more specifically to the refunding bondholders. The full jurisdiction and control over them is in this court. The refunding bondholders by an overwhelming majority do not consent. If the court has the power as a court of bankruptcy to consent for them, under the circumstances of this case it should refuse to do so. I do not think Congress intended to force a merger undesired by the majority in amount of the affected parties by permitting a merger to be part of a plan. ***

"This railroad property is in equity the property of the refunding bondholders who replace practically the stockholders as owners. On a reorganization they would naturally receive the common stock pro rata. All the plans approved by the Commission save the present one so provided. With that set-up it would not much matter what reorganization value and total capitalization was fixed; for the common stockholders would get the surplus earnings. ***

> "This case is not as though the merging corporations were affiliates, and members of the same corporate family already. In such a case there is really a mere simplification of corporate organization of interests already related. The Coast Line, though an unsecured creditor, is really a stranger in interest, having been found to have no interest in the railroad property to be reorganized."

Petitioners are informed that the legislative history referred to by Judge Sibley will be reviewed in other briefs. For that reason it is not reviewed here.

Petitioners' position is that the legislative history clearly and explicitly sustains and confirms the conclusion that the consistency clause limits the Commission's merger, consolidation and transfer powers to those conferred by the Interstate Commerce Act.

The basic reason for the limitation is that the power of Congress to provide for the relief and rehabilitation of financially distressed railroads flows from the bankruptcy power,[27] while the commerce power[28] is the source of the power to regulate mergers, consolidations and transfers, and the latter had been the subject matter of much controversy and legislation prior to the enactment of §77 in 1933.

Reading §77 as written, the unmistakable purpose and intent was to extend the "subject of bankruptcies" into a field not then occupied, by providing for the relief and rehabilitation of financially distressed railroads, but to preserve intact the existing national policy regulating mergers, consolidations and transfers.

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[27] Constitution, Article 1, §8, Clause 4: "The Congress shall have Power *** To establish *** uniform Laws on the subject of Bankruptcies throughout the United States ***."

[28] Constitution, Article 1, §8, Clause 3: "The Congress shall have Power *** To regulate Commerce *** among the several States ***."

"Obviously, §77 does no more than follow the line of historical and progressive development projected by previous acts"; its scope and purpose is "an adjustment of a failing debtor's obligations."[29] It is "bottomed upon the theory of debtor rehabilitation by adjustment of creditors' claims."[30] It was not designed as legislation empowering the Commission to receive or accept a stranger railroad's gratuitous offer to acquire the property of a debtor, or to make a counter-offer for acceptance or rejection.

There was good reason for this. Acting under the commerce power, and after fullest discussion and consideration through the years, Congress had formulated and matured the national policy regulating mergers, consolidations and transfers. The policy and the provisions to effectuate it were expressed in the Interstate Commerce Act. The Commission had for many years sought power to compel mergers, consolidations and transfers, but Congress had consistently refused to grant it. This history is reviewed fully in *Schwabacher v United States*, 334 US 182 (1948). It will not be repeated here.

Suffice it to say that in enacting §77 Congress demanded and received unqualified assurances that it would not enlarge the merger, consolidation or transfer powers of the Commission, and took every precaution to make certain that it did not. This it accomplished by expressly limiting the powers to those conferred by the Interstate Commerce Act.

It certainly cannot be thought that by the enactment of §77 in 1933, or by its revision in 1935, Congress intended to empower the Commission, through the processes of bankruptcy, to approve or authorize a merger, consolidation or transfer contrary to the Interstate Commerce Act. The

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29 *Continental Ill N B & T Co v Chicago R I & P R Co*, 294 US 648, 673 (1935)

30 *Ecker v Western P R Corp*, 318 US 448, 469 (1943)

consistency clause evidences the contrary intent—that any merger, consolidation or transfer provided for in a plan should be controlled by the "provisions" requiring that it be in harmony with and in furtherance of the nation-wide plan. That intent being obvious, there is no reason to think that Congress intended to require compliance with only that provision and to dispense with compliance with the one requiring the assent of "all the carriers involved."

The word "provisions" as used in the consistency clause is broad and all inclusive. There is nothing to indicate that Congress meant only one provision and not the other. The natural and logical conclusion is that Congress meant that a plan of reorganization could include only a merger, consolidation or transfer complying with the provisions requiring harmony with the nation-wide plan and assent by "all the carriers involved."

The combined consistency clause in §77(f) of the 1935 revision, like its two predecessors, requires consistency with both the "provisions and purposes" of the Interstate Commerce Act. Those provisions and purposes continue to encourage voluntary mergers, consolidations and transfers, and to permit their approval and authorization, but have never been enlarged to authorize compulsion.

The attitude of the commission majorities was that because the combined clause was transferred to §77(f), instead of being placed in §77(b) or elsewhere, it applies only to action by the Commission after confirmation of a plan, and no longer prohibits commission approval and certification of a plan providing for a merger, consolidation or transfer which is inconsistent with both the provisions and purposes of the Interstate Commerce Act. (267 ICC 731; IV, 731)

This attitude leads inevitably to one of two inadmissible results—either that because of its transfer to §77(f) the

combined consistency clause is meaningless; is to be read out of §77, and is to be given no effect, or that the Commission can approve and certify to the court a plan providing for a merger, consolidation or transfer which is inconsistent with the provisions and purposes of the Interstate Commerce Act, and the court can approve and confirm it, but the Commission then cannot grant authority to effectuate it.

It is unthinkable that the combined consistency clause can properly be read out of §77, and be given no effect. In the first place, if that had been the intent, Congress would not have gone to the trouble of combining its two predecessor clauses and including them in their combined form in the 1935 revision. Instead, it would have omitted both, and the 1935 revision would have been silent on the subject of consistency.

In the second place, when §77 was revised, the established national regulatory policy, which was not changed until five years later, was that the railroads of the nation be consolidated into the limited number of systems provided for in the nation-wide plan, and that this should be accomplished by voluntary consolidations assented to by all the carriers involved and in harmony with and in furtherance of the master plan. If the intent had been that the national policy should not apply to railroads in reorganization, and that a merger, consolidation or transfer involving a debtor and another railroad could conflict with the nation-wide plan, or that one in harmony with the nation-wide plan could be forced by the Commission without the "assent" of the debtor, Congress would have said so plainly. That meaning cannot be attributed to the combined consistency clause.

The other alternative—that the Commission can entertain, approve and certify to the court a plan providing

for a merger, consolidation or transfer which is inconsistent with the provisions and purposes of the Interstate Commerce Act, and the court can approve and confirm it, but the Commission then cannot grant authority to effectuate it—is equally inadmissible. The mere statement of the proposition refutes it. Congress should not be subjected to the accusation of having intended to authorize the Commission and court to labor in vain to produce, approve and confirm a plan which cannot be carried into effect.

The plain meaning of the combined consistency clause, regardless of its location in the 1935 revision, is that it is just as much a limitation on the merger, consolidation and transfer provisions in §77(b) as if it had been placed in that section. The fact that it is expressed in the form of a limitation on the powers exercisable by the Commission after confirmation does not govern its application. The application is that a merger, consolidation or transfer inconsistent with the provisions and purposes of the Interstate Commerce Act cannot be the "means for the execution" of a plan.

What the Commission cannot do after confirmation, it cannot do at any earlier stage of the proceeding. The Commission cannot approve or certify that which it cannot grant authority to effectuate.

A merger, consolidation or transfer may be included in a plan only as a means of execution. The Commission must determine that a merger, consolidation or transfer will be "consistent" before it can approve or certify a plan, otherwise the certified plan will be lacking in permissible means of execution.

Indeed, the obvious purpose in framing the combined consistency clause in the form of a limitation on the authority that the Commission can grant, is to make it a limi-

tation on all other provisions in §77—to make it plain that the Commission cannot, from the outset to the conclusion of the proceeding, take any action, or exercise any power, or entertain or consider any proposal, or approve or authorize any merger, consolidation or transfer, which is inconsistent with the provisions and purposes of the Interstate Commerce Act.

The combined consistency clause is a limitation which applies from the inception to the end of the proceeding. It limits the merger, consolidation and transfer powers of the Commission to those conferred by the Interstate Commerce Act, and those alone. In this case it prohibited the Commission from entertaining, as a complete plan of reorganization, Coast Line's unilateral offer to purchase debtor's property. It prohibited the approval and certification, as a plan of reorganization, of the commission majority's counter-offer to sell the property to Coast Line.

2. The 5% Bondholders Are Debtor's Equitable Owners and in That Capacity Are Entitled to Vote Under §5(11) of the Interstate Commerce Act on the Question of Corporate Assent by Debtor to the Merger, Consolidation or Transfer.

The commission majority argued: "The solvent corporation here is willing. There is nothing in the Interstate Commerce Act to prohibit us from approving such a transaction. *** There is nothing of record to show that the merger of the Florida East Coast with the Atlantic Coast Line is objected to by either. The stockholders of the Florida East Coast have not objected. The objection comes from certain of its bondholders." [31]

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31 Fourth Supplemental Report, 267 ICC 732; IV, 732. Cf., *Callaway v Benton*, 336 US 132, 138, footnote 6: "*** when the rights of bondholders of the lessor may be affected, as was the case with Terre Haute bondholders in the Milwaukee Railroad reorganization (see Group of

This overlooks the fact that debtor's "property is in equity the property" of the bondholders referred to, "who replaced practically the stockholders as owners." (81 F Supp 933) "It is expressly found that the debtor's insolvency is such that the stockholders are not interested parties. The debtor, its property and affairs now belong in equity to the creditors, and more specifically to the refunding bondholders." (81 F Supp 932) Because debtor's capital stock is without value and represents no equity or equitable ownership, and the 5% refunding bondholders are the senior class of creditors whose securities will not be paid in full, they are the equitable owners of debtor and its property. (VI, 588, 632, 682; 261 ICC 172; IV, 172; 267 ICC 756; IV, 756; 282 ICC 224; I, 224)

They became the equitable owners in 1932 when the trustees holding the mortgage securing payment of their bonds brought suit to foreclose it and had receivers of debtor appointed, or at the latest in 1941 when they instituted the proceeding for the reorganization of debtor under §77 of the Bankruptcy Act. (81 F Supp 928; 103 F Supp 828) They were as much the owners when their trustees brought the foreclosure suit and secured the receivership as if a decree of foreclosure had been entered and the property had been sold to them; the decree and the sale would have done nothing but recognize officially what had before been true in fact.[32]

Institutional Investors v Chicago M St P & P R Co, 318 US 523, 87 L ed 959, 63 S Ct 727, 52 Am Bankr NS 526, and discussion infra), nearly unanimous consent of such bondholders may be required before the changes can be made effective. The Interstate Commerce Commission took that position in the Milwaukee case and provided that the offer to Terre Haute should not be deemed accepted unless substantially all of its bondholders voted to accept. Chicago M St P & P R Co Reorganization, 239 Inters Com (F) 485, 536-538; 240 Inters Com (F) 257, 270, 271. See also 318 US at 532, 533, 87 L ed 989, 990, 63 S Ct 727, 52 Am Bankr NS 526."

32 *Helvering v Alabama Asphaltic Limestone Co*, 315 US 179, 183 (1942); *Bondholders Committee v Commissioner*, 315 US 189 (1942); *Helvering v Cement Investors, Inc*, 316 US 527, 532 (1942); *Helvering v New Haven & S L R Co*, 121 F2d 985, 987 (CA2, 1941)

They were as much the owners when they initiated the §77 proceeding as if debtor had been reorganized in what Judge Sibley called "the simple and natural manner several times certified by the Commission unanimously by giving all the refunding bondholders a pro rata share of its common stock" (81 F Supp 929); the receipt of the common stock pro rata would have done nothing but recognize officially what had before been true in fact.[33]

Helvering v Alabama Asphaltic Limestone Co, 315 US 179 (1942), dealt with the question whether creditors became equitable owners of a bankrupt's property when they instituted an involuntary bankruptcy proceeding to effectuate a plan of reorganization by a bankruptcy sale of the property to a new corporation, whose stock would be issued to the creditors in satisfaction of their claims, thus invoking and enforcing the full priority rule of the Boyd case[34] and excluding the bankrupt's stockholders from participation. The Court said (315 US 183):

> "Technically that did not occur in this proceeding until the judicial sale took place. For practical purposes, however, it took place not later than the time when the creditors took steps to enforce their demands against their insolvent debtor. In this case, that was the date of the institution of bankruptcy proceedings. From that time on they had effective command over the disposition of the property. The full priority rule of Northern P. R. Co. v. Boyd, 228 US 482, 57 L ed 931, 33 S Ct 554, applies to proceedings in bankruptcy as well as to equity receiverships. Case v. Los Angeles Lumber Products Co. 308 US 106, 84 L ed 110, 60 S Ct 1, 41 Am Bankr Rep (NS) 110. It gives creditors, whether secured or unsecured, the right to exclude stockholders entirely from the reorganization

33 Cases cited footnote 32

34 *Northern P R Co v Boyd*, 228 US 482 (1913)

plan when the debtor is insolvent. See Re 620 Church Street Bldg. Corp. 299 US 24, 81 L ed 16, 57 S Ct 88, 32 Am Bankr Rep (NS) 185. When the equity owners are excluded and the old creditors become the stockholders of the new corporation, it conforms to realities to date their equity ownership from the time when they invoked the processes of the law to enforce their rights of full priority. At that time they stepped into the shoes of the old stockholders. The sale 'did nothing but recognize officially what had before been true in fact.' Helvering v. New Haven & S. L. R. Co. (CCA 2d) 121 F (2d) 985, 987."

In *Helvering v Cement Investors, Inc*, 316 US 527 (1942), the court considered the question whether owners of first mortgage bonds became equitable owners of the mortgaged property when the company filed a §77B petition under which a reorganization was effected by transfer of the property to a new company, which issued income bonds and common stock in exchange for the old bonds, but gave the stockholders of the debtor no interest in the new company except that in exchange for the stock they received warrants for the purchase of new shares. In deciding that question the court said (316 US 532):

"In case of reorganizations of insolvent corporations the creditors have the right to exclude the stockholders entirely from the reorganization plan. When the stockholders are excluded and the creditors of the old company become the stockholders of the new, 'it conforms to realities to date their equity ownership' from the time when the processes of the law were invoked 'to enforce their rights of full priority.' Helvering v. Alabama Asphaltic Limestone Co. 315 US 179, ante, 775, 62 S Ct 540. Under that approach the ownership of the equity in these debtor companies effectively passed to these creditors at least when §77B proceedings were instituted."

The opinion in *Helvering v New Haven S L R Co*, 121 F2d 985 (CA 2, 1941) was by Judge Learned Hand. The controlling point was whether bondholders became equitable owners of mortgaged property on the date their trustee filed a state court bill to foreclose the mortgage securing payment of the bonds, and a reorganization was effected by foreclosure sale of the property to a bondholders committee, followed by the committee's transfer of the property to a new company in consideration of the issuance of the new company's common stock to the old bondholders. Speaking for the court, Judge Hand said (121 F2d 987):

> "Debts are payable in money and give creditors neither power to control the debtor's property, nor any concern with its vicissitudes while the debtor remains solvent; they do not share in his gains, or suffer from his losses. *** This ceases, however, as soon as the debtor becomes irrecoverably insolvent and the debts are due; the creditors are then entitled to control the property, and thereafter its adventures are their own. The debtor loses any rightful power to dispose of it except for an adequate price, and courts like to speak of him as a 'trustee'; all that is necessary to make them complete legal owners is that they shall follow the prescribed legal formalities. *** the bondholders were as much the owners before foreclosure as after; the decree and the sale did nothing but recognize officially what had before been true in fact."

Thus, in the instant case, the 5% bondholders "stepped into the shoes" of debtor's stockholders either in 1932, when their trustees brought the foreclosure suit and secured the receivership, or in 1941, when they instituted the §77 proceeding. They have at all times since one or the other of those events been in the shoes of debtor's stockholders.

In those shoes, and in the exercise of the rights acquired by stepping into them, they are entitled to vote under §5(11) of the Interstate Commerce Act on the question of corporate assent by debtor to the proposed merger, consolidation or transfer. The proposed merger, consolidation or transfer cannot be forced or effectuated without "the assent *** of a majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the" 5% bonds. (§5(11))

This can be illustrated by assuming that the 5% bondholders instituted the §77 proceeding because of insolvency not in the bankruptcy sense of liabilities exceeding assets, but in the equity sense of debtor being "unable to meet its debts as they mature." (§77(a)) That would mean either that the value of assets in excess of liabilities would impart value to debtor's capital stock, or that the value of the assets would at least equal liabilities and value would attach to the capital stock upon debtor becoming able to meet its debts as they mature.

In either event, the fact that the stock represented value and equitable ownership would mean that the stockholders would continue to have rights, one of which would be the right to vote on the question of merger, consolidation or transfer. No one would contend in this situation that the mere pendency of a §77 proceeding would invest the Commission with power to approve or certify a plan of reorganization providing, without the assent and over the objections of the stockholders, for a merger, consolidation or transfer resulting from the Commission's having entertained and considered another railroad's offer to acquire debtor's property, and the acceptance by the other railroad of a Commission counter-offer to dispose of it. No one would be so bold as to urge that the assent of the stockholders would not be required under §5(11) of the Interstate Commerce Act.

Two separate votes, at different times, on different questions, and in different capacities, would be required. The first, to be taken before the Commission could approve or certify the plan, would be the group vote of stockholders at a regular or special meeting, under §5(11) of the Interstate Commerce Act, on the question of corporate assent to the merger, consolidation or transfer. The second, to be taken after approval and certification of the plan by the Commission and its approval by the court, would be the individual action of each affected creditor and stockholder, under §77(e) of the Bankruptcy Act, on the question of acceptance or rejection of the plan.

The vote of the stockholders at such a meeting would be their group or collective vote, in the capacity of stockholders, on the question of authorizing or not authorizing corporate action. It would be a part of the corporate mechanics by which the corporate assent to a merger, consolidation or transfer agreement would be given or withheld. It would have nothing to do with acceptance or rejection of the plan of reorganization.

Acceptance or rejection of the plan by each creditor and stockholder would be his individual act in the capacity of a person affected. The acceptance or rejection would not be given at any stockholders or other meeting, regular or special, and would not be a group or collective vote. The individual acceptances or rejections would not authorize or refuse to authorize any corporate action. They would have nothing whatever to do with corporate action. They would neither give nor withhold corporate assent to any merger, consolidation or transfer agreement.

The vote of the stockholders at a regular or special meeting would be required because they would be debtor's equitable owners. Here, the 5% bondholders are in fact the equitable owners. To say that the right to vote on the question of merger, consolidation or transfer is con-

trolled by the technicality of stock-ownership, as against bond-ownership, rather than by equitable ownership, would sacrifice substance to form.

3. The "Cram-Down" Provision in §77(e) of the Bankruptcy Act Conferred No Power on the Commission.

The commission majority relied on the so-called "cram-down" provision in §77(e). It argued: "Any contention that the merger must be voluntary is nullified by the 1935 amendment to section 77, which provides, in subsection (e) that 'if the plan has not been accepted by the creditors and stockholders, the judge may, nevertheless, confirm the plan over their objection.' This provision is not restricted to any one of the several plans authorized in subsection (b). It refers to any plan authorized by that subsection. Subsection (b) specifically authorizes a plan which may provide for the merger of the debtor corporation with another corporation. Any involuntary aspects of such merger fade completely in the face of the power of the court to confirm the plan providing for such merger over the objection of creditors or stockholders."[35]

A patent fallacy in this argument is that the cram-down provision relates solely to the powers and functions of the court. It gave the court, but not the Commission, a new power. It did not give the Commission power to approve or certify a plan of reorganization providing for a merger, consolidation or transfer "inconsistent with the provisions and purposes of the Interstate Commerce Act." It did not give the Commission power to approve or certify a plan providing for a merger, consolidation or transfer to which debtor's equitable owners do not assent but object.

The reasoning of the commission majority involved this thought process: (1) After a plan certified by the Com-

35 Fourth Supplemental Report, 267 ICC 732; IV, 732

mission has been approved by the court and rejected by some classes of interested parties, the court may nevertheless confirm it under specified circumstances and conditions; (2) therefore, before the Commission certifies a plan, it may approve one providing for a merger, consolidation or transfer which would be unauthorized if the court did not have the power of confirmation notwithstanding rejection; (3) therefore, the conferring on the court of power to confirm notwithstanding rejection released the Commission from the congressional mandate that it can approve and authorize only carrier-initiated, voluntary mergers, consolidations and transfers which are assented to by the equitable owners of each railroad involved; (4) therefore, the Commission can approve and certify a plan providing, without the consent and over the objections of debtor's equitable owners, for a merger, consolidation or transfer resulting from the Commission's having entertained another railroad's offer to purchase debtor's property, and the acceptance by the other railroad of a Commission counter-offer to sell it; (5) therefore, the Commission can approve and certify an unauthorized plan on the assumption that, notwithstanding the objections of debtor's equitable owners, the court can and will cram it down their throats.

The short answer is that the cram-down provision conferred no power whatever on the Commission.

It did not enlarge, reduce or affect the powers of the Commission.

It authorized no commission action.

It did not repeal or modify the requirement that if a merger, consolidation or transfer is to be the means for the execution of a plan, the merger, consolidation or transfer must be consistent with the "provisions and purposes" of the Interstate Commerce Act.

4. The Court's "Cram-down" Power Does Not Authorize Confirmation of the So-called "Forced Merger" Plan of Reorganization.

In an attempt to fortify its previous dogmatic statements, and far in advance of the event, the prevailing opinion in the Court of Appeals holds that after the anticipated rejecting vote of the 5% bondholders, the "forced merger" plan must be confirmed unless "conditions should so change" as to render it no longer "fair and reasonable." (201 F2d 330-331) Thus, by a gratuitous and completely erroneous construction of the cram-down provision in §77(e), and without noticing or referring to the combined consistency clause, the court of appeals majority adopted and approved the contention of the commission majority that it could approve and certify a plan providing for a merger, consolidation or transfer violating both the provisions and purposes of §5 of the Interstate Commerce Act, and the court could and would cram it down the 5% bondholders' throats.

Since the Commission did not have power to approve or certify to the court the so-called "forced merger" plan, it was never properly before the court. Consequently, although Judge Strum disapproved it on other grounds, the disapproval was right, and the Court of Appeals was wrong in reversing and directing that it be approved. The Commission's lack of power to approve and certify the plan vitiates everything done subsequently.

A plan cannot be submitted to a debtor's affected creditors and equitable owners, for acceptance or rejection, until after the Commission has properly approved and certified it to the court, and the court has approved it. The so-called "forced merger" plan has never achieved that status, and can never do so. Therefore, it can never be submitted to debtor's affected creditors and equitable

owners, for acceptance or rejection, and the jurisdiction of the court to decide whether it should be confirmed notwithstanding rejection can never be invoked or exercised.

Aside from the foregoing, the court's "cram-down" power applies solely to the second vote to be taken in connection with a plan providing for a merger, consolidation or transfer—the individual vote of each affected creditor or equitable owner, to be taken under §77(e) of the Bankruptcy Act, on the question of acceptance or rejection of a plan which has been properly approved and certified by the Commission and approved by the court. It does not apply to the first vote to be taken on such a plan—the group vote of equitable owners at a regular or special meeting, on the question of corporate assent to the merger, consolidation or transfer, to be taken under §5(11) of the Interstate Commerce Act, before the Commission can approve or certify the plan.

The two votes are on wholly different questions. They are by persons acting in completely different capacities. The factors and considerations governing them are entirely unrelated.

The second vote, which is not taken at any meeting, calls for individual acceptance or rejection of the plan by each affected creditor and equitable owner. The Commission takes this vote by submitting the plan, together with its reports or summaries and the opinion and order of the judge, to each affected creditor and equitable owner. (§77(e)) The question decided by the sum of their individual acceptances or rejections involves factors and considerations which have long been within the equity and bankruptcy jurisdictions of courts—fair and equitable treatment, due recognition of rights of classes of creditors and stockholders, unfair discrimination in favor of classes of creditors or stockholders, conformity to the require-

ments of the law of the land regarding the participation of the various classes of creditors and stockholders, and reasonable justification for rejective action in the light of all the relevant facts and the respective rights and interests of those rejecting.

The first vote, the vote on the question of corporate assent to the merger, consolidation or transfer, is not by creditors and equitable owners, but is limited to equitable owners alone. It is not taken by submitting a question to each equitable owner individually, but is a group or collective vote at a regular or special meeting of the equitable owners. It does not relate to acceptance or rejection of the plan. Instead, it relates to the authorization or non-authorization of corporate action. It involves factors and considerations which have always been in the realm of business judgment and decision, and not within the equity, bankruptcy or other jurisdiction of courts—corporate assent to a merger, consolidation or transfer agreement voluntarily negotiated through the process of arm's length bargaining by a seller or sellers willing but not compelled to deal or sell, and a purchaser or purchasers desirous but not compelled to deal or buy.

These separate procedures, at the different times, are required by the combined consistency clause. Its overall effect is that if a plan provides a merger, consolidation or transfer as its means of execution, the means must be authorized by appropriate corporate action independent of acceptance or rejection of the plan by those whom it will affect.

This was ignored by the commission and court of appeals majorities. They seek to short-circuit the requirement of corporate authorization by treating the "means" as the "end," and assert that without corporate authorization or assent, a merger, consolidation or transfer can be

crammed down the throats of equitable owners. The reason for their beclouded vision is that in this instance the proposed merger, consolidation or transfer is not utilized as the means for the execution of an otherwise fair and equitable plan, but was conceived, proposed and approved as the sole and only purpose, objective and end of the plan.

They propose to accomplish the short-circuiting under the cram-down provision, but lose sight of the fact that it does not apply to the vote on the question of corporate authorization of assent to a merger, consolidation or transfer. It is not the function of courts, nor within their jurisdiction, to determine or decide what is best for owners in regard to keeping or selling property they have chosen and lawfully own. A fundamental concept of our system of government is that what a man chooses to own, if lawful, cannot be taken away from him in consideration of something that a court thinks is as good or better, except under the power of eminent domain.

The cram-down provision authorizes confirmation of an unreasonably rejected plan which has been approved by both Commission and court. It does not authorize the court to cram down the throats of equitable owners a proposed merger, consolidation or transfer which they, in the exercise of their business judgment, have concluded and decided is unsatisfactory and objectionable to them, and to which they do not assent or agree.

The purpose of the cram-down provision is to prevent dissident minorities from blocking confirmation of a plan approved by Commission and court—to obviate the exacting of inequitable adjustments by obstructive minorities as the price of their consents. Because the acceptance of the holders of two-thirds in amount of the claims of any class binds the remainder of the class, and becomes the acceptance of the entire class, the dissident

or obstructive minorities obviously cannot be and are not minorities within a class. Instead, they are minorities in the sense of inferior classes in a complicated financial structure. That situation does not exist here.

The commission and court of appeals majorities propose that the cram-down clause be used against debtor's equitable owners, although they are not an inferior; but are the senior and only interested class. The use proposed is to cram down their throats, not a plan which provides for rehabilitating debtor by scaling down indebtedness to bring it within ability to pay and issuing to the senior class of creditors new securities of the same enterprise in exchange for those now held, but one which provides for a merger, consolidation or transfer that is unsatisfactory and objectionable to them, as debtor's equitable owners, and to which, in the exercise of their business judgment, they do not assent or agree.

This would extend the scope of the bankruptcy power into the field of eminent domain, contrary to the inhibitions of the Fifth Amendment. To so use the cram-down provision would permit the taking of the bondholders' property by Coast Line—as much so and with identically the same effect as if Coast Line had proceeded directly under Rule 71A of the Federal Rules of Civil Procedure, by bringing an action in the district court to condemn debtor's property, had such a proceeding been possible.

The only differences would be that in the condemnation action Coast Line would be required (1) to pay compensation equal to the fair value of the property and, (2) to pay the compensation in money; but the cramming down of the proposed merger, consolidation or transfer would permit Coast Line (1) to pay only debtor's so-called "reorganization value" and, (2) to deliver its securities in payment of 91% of that value. This would be contrary to all concepts of due process and just compensation.

By whatever name it is called, and whatever may be the excuse for it, the end result of the "forced merger" would be to take from the 5% bondholders their private property and vest it in Coast Line, forcing them to accept compensation payable 91% in unwanted Coast Line securities. The bankruptcy power of Congress does not empower that taking, nor is it authorized by the power of Congress to regulate interstate commerce.

The bankruptcy power is not susceptible of final definition, its scope being the "subject of the relations between an insolvent or nonpaying or fraudulent debtor, and his creditors, extending to his or their relief."[36] Nevertheless, "The bankruptcy power, like all the other great substantive powers of Congress, is subject to the Fifth Amendment."[37] That amendment prohibits the taking of private property for other than public use, and for public use permits a taking only by "due process of law" and upon payment of "just compensation."

As reviewed in the cited cases, the history and development of the Bankruptcy Act disclose that its original purpose was to effect ratable distribution among creditors of the property of an insolvent, non-paying or fraudulent debtor. It was later extended to relieve the honest debtor from oppressive indebtedness and permit him to start afresh. It has not been, it could not be, extended to primarily benefit a covetous purchaser of the insolvent estate. If that could be done, Congress could authorize initiation of a bankruptcy proceeding by a stranger seeking to acquire the property of an insolvent debtor, and thereby deprive the debtor and his creditors, not only of their property, but also of their right to work out a voluntary adjustment in their relations.

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36 *In re Reiman*, DC NY, Fed Case No 11,673 (1874); *Wright v Union Central Life Ins Co*, 304 US 502 (1938); *United States v Bekins*, 304 US 27 (1938); *Continental Ill N B & T Co v Chicago R I & P R Co*, 294 US 648 (1935); *Hanover Nat'l Bank v Moyses*, 186 US 181 (1902)

37 *Louisville Joint Stock Land Bank v Radford*, 295 US 555 (1935)

When a creditor and his debtor enter into a contract creating the relationship, they make it subject to the bankruptcy power to modify it for the benefit and relief of the debtor, to the detriment of the creditor. That is a part of their contract. The power to take from the creditor for the benefit and relief of the debtor is within the "subject of bankruptcies."[38] But when the debtor-creditor relationship is created, they do not contract subject to any power of modification in favor of a stranger to the contract, to their mutual detriment, nor do they contract subject to any power of modification in favor of an unsecured creditor to the detriment of secured creditors. Conferring a benefit upon a stranger at the expense of creditors, or upon an unsecured creditor at the expense of secured creditors, is not within the "subject of bankruptcies."

Railroads are privately owned, even though their property be devoted to public use. This Court has held[39] that railroad property is

> "*** entitled to the protection of the Constitution, and in the precise manner in which protection is given. It can only be taken by the exercise of the power of eminent domain; and a condition precedent to the exercise of such power is *** that the statute conferring it make provision for reasonable compensation to the owner of the property taken."

The power of Congress to regulate interstate commerce is derived from Article 1, §8, Clause 3, of the Constitution. That power can only be exercised in subjection to the guaranty of due process.[40] In the cited case this Court said:

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38 *Louisville Joint Stock Land Bank v Radford*, 295 US 555 (1935); *Wright v Union Central Life Ins Co*, 304 US 502 (1938)

39 *Western Union Telegraph Co v Pennsylvania R Co*, 195 US 540, 570 (1904)

40 *Railroad Retirement Board v Alton R Co*, 295 US 330 (1935)

"This court has repeatedly had occasion to say that the railroads, though their property be dedicated to public use, remain the private property of their owners, and that their assets may not be taken without just compensation. The carriers have not ceased to be privately operated and privately owned, however much subject to regulation in the interest of interstate commerce. *There is no warrant for taking the property of one and transferring it to another* without compensation, whether the object of the transfer be to build up the equipment of the transferee or to pension its employees." (295 US 357—Emphasis supplied)

Under the Commerce Clause, Congress has power to prescribe rules by which interstate commerce shall be regulated.[41] Nevertheless, the power of regulation is not absolute, but is limited by the constitutional guaranty that no person shall be deprived of his property without due process of law.[42]

Under no circumstances can the 5% bondholders' private property be taken in the manner and for the compensation provided. Even if taken for public use under the power of eminent domain, the Fifth Amendment requires the payment of just compensation, which must be made only and solely in money. All other proposed mediums of payment have been stricken down as unconstitutional.[43] And a taking which cannot be authorized under the power of eminent domain cannot be authorized under any other power.

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41 *Gibbons v Ogden*, 9 Wheat 1, 196 (1824)

42 *United States v Chicago, M St P & P R Co*, 282 US 311 (1931)

43 18 Am Jur, Eminent Domain, §128; 3 Nichols on Eminent Domain (3 ed) §8.2; 29 CJS, Eminent Domain, §191b; Lewis on Eminent Domain (3 ed) §§ 682, 756

If the 5% bondholders are to be deprived of their private property, the only method by which it can constitutionally be taken is by the exercise of the power of eminent domain. That great power authorizes a taking of private property for "public use," but does not authorize a taking in the "public interest,"[44] as the "forced merger" plan proposes.

Debtor has been judicially declared to be engaged in "public use."[45] Since it is already in public use as an operating railroad, the taking cannot be justified on the basis that debtor would be acquired for public use. Property devoted to one public use may be taken for a different and higher public use, but private property devoted to public use cannot be taken by another for the same public use.[46] The only purpose for which Coast Line seeks to acquire debtor is to continue to operate it for identically the same public use in which it is now being operated.

The end result of merger, consolidation or transfer would be to vest in Coast Line railroad property devoted to public use already, and Coast Line would operate it not for a different, but for the same, public use. The only real change would be that operating profits would thereafter inure to the benefit of Coast Line rather than debtor's 5% bondholders.

Courts of all jurisdictions have been impressively emphatic and uniform in holding that private property dedi-

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44 18 Am Jur, Eminent Domain, §37

45 *Florida East Coast Ry Co v Shaw*, 11 F2d 653 (1926)

46 18 *Am Jur, Eminent Domain*, §97; 1 *Nichols on Eminent Domain* (3 ed) §2.2(8); *West River Bridge v Dix*, 6 How 507 (1848); *Boston Water Power Co v Boston & W R Corp*, 40 Mass 360 (1839); *Cary Library v Bliss*, 151 Mass 364, 25 NE 92, 7 LRA 765 (1890); *Lake Shore & M S Ry Co v Chicago & W I R Co*, 97 Ill 506 (1881); *Long Island Water Supply Co v Brooklyn*, 166 US 685 (1897—distinguishing between the State itself taking a public utility rather than another private corporation)

ated to "public use" cannot be taken for the same public use. This Court said at an early date:[47]

> "Nor could this bridge have been taken by the State, and kept up by it, as a toll bridge. This could not be called an appropriation of private property to public purposes. *There would be no change in the use, except the application of the profits,* and this would not bring the act within the power. The power must not only be exercised bona fide *** but the property, not its product, must be applied to public use.
>
> "It is argued that if the State may take this bridge, it may transfer it to other individuals, under the same or a different charter. This the State cannot do. It would in effect be taking the property from A to convey to B." (Emphasis supplied)

In *Elkins Elec R Co v Western Maryland R Co*[48] the District Court held:

> "It must be conceded that, where one railroad company has secured under its charter rights the right of way and built thereon its line of road and is using the same for public uses, the Legislature could not authorize the taking wholly thereof by another railroad corporation for a like public use."

In a case[49] wherein counsel argued that if property "has already been appropriated to public use, and is, in fact, in such use in the hands of one corporation, it cannot be rightfully taken (even by the authority of a statute to that effect) away from such corporation, for the purpose of subjecting it to the same public use in the hands of another corporation," the Illinois Supreme Court conceded that to be true, since

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47 *West River Bridge v Dix*, 6 How 507, 537 (1848)

48 163 F 724, 732 (1908), affirmed 186 F 1022 (1911), certiorari denied 223 US 725 (1911)

49 *Lake Shore & M S Ry Co v Chicago & W I R Co*, 97 Ill 506 (1881)

"where the public use in question is *the same*, such taking would undoubtedly degenerate into a taking from one for the mere purpose of giving to another, which we hold (under our institutions) is not within the domain of legislative power." (Emphasis supplied)

The Supreme Court of Washington[50] held that property devoted to public use by a public service corporation

"cannot be taken to be used for the same purpose in the same manner, as that would amount simply to a taking of property from one and giving it to another, without any benefit or advantage whatever to the public—an act which the legislature is powerless to authorize."

To like effect the courts of Oregon,[51] Texas,[52] Pennsylvania[53] and Massachusetts[54] have held that property devoted to public use may not be taken from the owner and delivered to another to be used for the same purpose.

This case is the first in which any section of the Bankruptcy Act has been construed as authorizing an unsecured creditor or stranger to expropriate the security underlying senior claims. That would be the effect of the "forced merger." It would permit the owners of senior liens to be deprived of their seniority without either the payment of their debt or the exercise of their right in equity, and under the mortgage, to a public foreclosure sale at which they may bid their debt.

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50 *Samish Boom Co v Union Boom Co*, 32 Wash 586, 73 P 670, 672 (1903); *Harbor Boom Co v Superior Ct Pac County*, 65 Wash 129, 117 P 755 (1911)

51 *Oregon Cascade R Co v Bailey*, 3 Or 164 (1869)

52 *Sabine & E T Ry Co v Gulf & I Ry Co*, 92 Tex 162, 46 SW 784 (1898)

53 *Sharon Ry Appeal*, 122 Pa St 533, 17 A 234, 9 Am St Rep 133 (1888); *Cleveland & P R Co, Petitioner*, 2 Pittsb R 348 (Pa, 1862)

54 *Boston Water-Power Co v Boston & W R Corp*, 40 Mass 360 (1839)

Petitioners urge that the Fifth Amendment prohibits ny such enlargement of the bankruptcy power. They ubmit that the cramming down of the proposed merger, onsolidation or transfer, to permit Coast Line to take heir property at a price which has never been determined be its fair value, for consideration which is not payable cash, would violate the Fifth Amendment.

Because Congress intended constitutional application of he cram-down provision, it should not be given the unonstitutional application proposed by the commission and ourt of appeals majorities.

The 1935 Amendments to §77 Do Not Authorize the "Forced Merger," Because the Inclusion in §77(e) of the Boyd Case "Fair and Equitable" Standard Requires the Retention of Creditors' Property Rights as in Equity Receiverships and Precludes Their Divestment by "Forced Merger."

Three basic rules apply in interpreting §77:

1. Reorganizations are not compositions.[55]

2. Reorganizations are intended to avoid, not foster, iquidations and thus are distinguishable from ordinary ankruptcies.[56]

3. "*** a proceeding under §77 is not an ordinary proeeding in bankruptcy. It is a special proceeding which eeks only to bring about a reorganization ***."[57]

Since reorganizations are neither ordinary bankruptcies nor compositions, the statutes authorizing them should not be interpreted as though they were. Section 77 must be

55 *Case v Los Angeles Lumber Products Co*, 308 US 106 (1939).

56 *Reconstruction Finance Corp v Denver & R G W R Co*, 328 US 495, 506, 509 (1946); *Fidelity Assurance Assn v Sims*, 318 US 608 (1943).

57 *Continental Illinois N B & T Co v Chicago R I & P R Co*, 294 US 648, 676 (1935).

examined in the light of its purpose which, in at least one respect, appears unmistakably in the language used.

The inclusion in §77(e) of the Boyd case "fair and equitable" standard is a congressional command that in railroad reorganizations creditors shall retain, within their respective classes, all rights in the debtor's property that they would have had in an equity receivership. Retention of the property rights is inconsistent with their divestment by "forced merger." Since the two cannot stand together —retention and divestment—Congress expressly authorized retention, which, of necessity, forbids divestment by "forced merger."

The "full and absolute priority rule" of the Boyd case is made applicable to railroad reorganizations by the §77(e) provision that the plan must be "fair and equitable." The rule has been restated by this Court in clear and unmistakable terms:[58]

> "The rule of the Boyd Case 'protects the rights of senior creditors against dilution either by junior creditors or by equity interests.' ***
>
> "Unless that principle is respected, there will be serious invasions of the rights of senior claimants to the benefit of junior interests. The property of one group will be subtly appropriated to pay the claims of another while lip service is rendered the principles of priority."

Thus before any non-creditor, or creditor of an inferior class, can obtain or retain an interest in the reorganized debtor, any new securities offered the senior class of creditors must be "of a value equal to the creditors' claims."[59] The rule is that "junior claims can receive nothing until

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[58] *Institutional Investors v Chicago, M St P & P R Co*, 318 US 523, 569, 570 (1943)

[59] *Consolidated Rock Products Co v DuBois*, 312 US 510, 530 (1941)

the senior claims receive securities of a worth or value *equal to their indebtedness.*"[60] (Emphasis supplied) It requires that "senior claims first receive securities of a worth *sufficient to cover their face and interest* before junior claims receive anything."[61] (Emphasis supplied)

In any construction of the language of §77 the primary consideration is the congressional intent pointedly evidenced by the inclusion in §77(e) of the full and strict priority rule of equity receiverships. That rule was not founded on empirical or utilitarian concepts growing out of the ravages of severe economic depression. The Boyd case was heard in November 1912 and decided in April 1913.[62] Its forerunners, dating back at least to 1868,[63] were decided over a wide range of business conditions.

The rule of the Boyd case was founded on *the property rights of creditors*,[64] as those rights were known and un-

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60 *Reconstruction Finance Corp v Denver & R G W R Co*, 328 US 495, 517 (1946)

61 *Ecker v Western Pacific R Corp*, 318 US 448, 483 (1943). Of course, the stockholders of an insolvent corporation may buy back into the reorganized, debtor—in effect re-purchase its ownership; but they cannot do so with contributions which are so inadequate as to dilute creditors' rights. Thus those who make necessary fresh investments may receive in return only participations reasonably equivalent to their contributions. (*Case v Los Angeles Lumber Products Co*, 308 US 106, 121, 122) But this does not apply to an inferior creditor class. They have never had any ownership interest subject to being "bought back."

62 A peak in the business cycle occurred in January 1913, following a low in January of 1912. The next business cycle trough did not occur until December 1914. *Historical Statistics of the United States, 1789-1945*, published by the Department of Commerce, at page 320.

63 "It has been stated, in all correctness, that the absolute priority doctrine is 'fundamentally conservative' and that it 'seeks to preserve our capitalistic system by protecting the investor so that the system will work.' Frank, Epithetical Jurisprudence and the Work of the Securities and Exchange Commission in the Administration of Chapter X of the Bankruptcy Act (1941) 18 N.Y.U.L.Q. Rev. 317, 340. In its insistence upon the strict recognition of traditional priorities, the absolute priority rule as Professor Dewing has indicated simply reiterates what the Supreme Court said as long ago as in that conservative era of Chicago, Rock Island & Pacific R. Co. v. Howard, [7 Wall 392 (1868)] 2 Dewing, Financial Policy of Corporations (4th ed. 1941) 1366, footnote o." 6 *Collier on Bankruptcy* (14 ed) p. 3872, n. 48

64 *Northern Pacific R Co v Boyd*, 228 US 482 (1913); *Case v Los Angeles Lumber Products Co*, 308 US 106 (1939)

derstood over the long history of equity receiverships.[65] They are the substantive rights of mortgage creditors summarized in *Louisville Joint Stock Land Bank v Radford*, 295 US 555, 594, 595 (1935).[66]

Congress wrote those substantive rights into §77 by including in §77(e) the Boyd case "fair and equitable" standard. In an opinion by Mr. Justice Douglas, this Court unanimously determined just what the sum total of those rights means in terms of equitable ownership of a debtor's property.[67] It was there decided that when creditors brought an involuntary bankruptcy proceeding to effect a reorganization plan enforcing the absolute priority rule, then —

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[65] The determination of the mortgagee's "priority" in terms of vested property rights during the growth of the full and strict priority rule is well set out in the following quotation from Mr. Justice Brewer in *Kneeland v American Loan and Trust Co of Boston*, 136 US 89, 97-98 (1890): "Upon these facts we remark, first, that the appointment of a receiver vests in the court no absolute control over the property, and no general authority to displace vested contract liens. Because in a few specified and limited cases this court has declared that unsecured claims were entitled to priority over mortgage debts, an idea seems to have obtained that a court appointing a receiver acquires power to give such preference to any general and unsecured claims. It has been assumed that a court appointing a receiver could rightfully burden the mortgaged property for the payment of any unsecured indebtedness. Indeed, we are advised that some courts have made the appointment of a receiver conditional upon the payment of all unsecured indebtedness in preference to the mortgage liens sought to be enforced. Can anything be conceived which more thoroughly destroys the sacredness of contract obligations? One holding a mortgage debt upon a railroad has the same right to demand and expect of the court respect for his vested and contracted priority as the holder of a mortgage on a farm or lot. So, when a court appoints a receiver of railroad property, it has no right to make that receivership conditional on the payment of other than those few unsecured claims which, by the rulings of this court, have been declared to have an equitable priority. No one is bound to sell to a railroad company or to work for it, and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility, and not in expectation of subsequently displacing the priority of the mortgage liens. It is the exception and not the rule that such priority of liens can be displaced. We emphasize this fact of the sacredness of contract liens, for the reason that there seems to be growing an idea that the chancellor, in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens."

[66] *In re Utilities Power & L Corp*, 29 F Supp 763, 769 (DC Ill, 1939)

[67] *Helvering v Alabama Asphaltic Limestone Co*, 315 US 179 (1942)

"From that time on they had effective command over the disposition of the property." (315 US 183)

Thus, whether and to what extent §77 might have constitutionally modified mortgage creditors' rights, should not be a problem here. When the "fair and equitable" standard was written into §77(e) at least sufficient of the mortgage creditors' substantive property rights were preserved to assure their retention of "effective command over the disposition" of debtor's property.

A "forced merger" necessarily violates those substantive property rights. It would render futile and ineffective the equitable owners' command over the disposition of the property. It would susbtantially invade and violate the entire bundle of property rights preserved to equitable owners by §77(e). It would be in irreconcilable conflict with the full and absolute priority rule.

In the face of the explicit congressional inclusion of that rule in §77(e) no mere inference that Congress intended to permit a "forced merger" can prevail. There never has been, and is not now, any basis for reading any such inference into §77.

The insistence of Congress on the application of the full and absolute priority rule to railroad reorganizations forecloses any intention to permit a "forced merger." The very nature of a "forced merger" contemplates results permissible only under the composition or liquidation theories, but §77, like Chapter X, rejected the composition theory "in favor of the full priority rule of the Boyd case."[48] This was shown with sparkling clarity in *Case v Los Angeles Lumber Products Co*, 308 US 106, 119, footnote 14 (1939), which says:

[48] *Marine Harbor Properties v Manufacturers Trust Co*, 317 US 78, 86 (1942); *Case v Los Angeles Lumber Products Co*, 308 US 106, 118 (1939)

"The statutory scheme of § 77B (in those respects which are material here) is in sharp contrast to that which was provided for compositions under former § 12. This court said in Callaghan v. Reconstruction Finance Corp. 297 US 464, 470, 80 L ed 804, 809, 56 S Ct 519, 30 Am Bankr Rep (NS) 446: 'Reorganizations now permitted under § 77B present certain resemblances to compositions under § 12, which have been commented upon as supporting the constitutionality of the reorganization provisions of § 77 or § 77B . . . But § 77B contemplates a procedure and results not permissible under § 12. Reorganizations are nowhere referred to in the statute as compositions.' Under § 12(a) (as it existed at the time § 77B was enacted) only a 'bankrupt' could offer 'terms of composition to his creditors.' Under § 77B(d) plans may be proposed not only by the debtor but also by a designated percentage of the creditors or, where the debtor is not found to be insolvent, by a specified percentage of stockholders. Section 12(d) as it then existed provided that the judge 'shall confirm a composition if satisfied' inter alia that 'it is for the best interests of the creditors.' See Fleischmann & Devine v. Saul Wolfson Dry Goods Co. (CCA5th) 299 F 15, 4 Am Bankr Rep (NS) 1028. The 'fair and equitable' standard employed in § 77B was not then present in § 12. Consent by the debtor to the composition was implicit in former § 12 (cf. Re Bryer (CCA2d) 281 F 812, 49 Am Bankr Rep 32). But under § 77B approval of a plan by security holders who have no equity in the enterprise is unnecessary. Re 620 Church Street Bldg. Corp. 299 US 24, 81 L ed 16, 57 S Ct 88, 32 Am Bankr Rep (NS) 185. The general view was well expressed in Re Dutch Woodcraft Shops (DC) 14 F Supp 467, 469, 30 Am Bankr Rep (NS) 351. 'The preservation of business enterprises must not be at the expense of

creditors, and the provisions of §77B should not be taken advantage of to effect what, in fact, amounts to a composition under §12.'"

Insistence by Congress on the full and absolute priority rule is established not only by the "fair and equitable" provision in §77(e) but also by the 1952 amendments to the Bankruptcy Act. By those amendments Congress wrote the rule out of the "composition" sections of the Act (Chapters XI, XII and XIII) but retained it in the reorganization provisions.[69]

That in the reorganization sections Congress also rejected the liquidation theory, whether by "forced merger" or otherwise, and rejected it in favor of the full and absolute priority rule, is established by *Fidelity Assurance Assn v Sims*, 318 US 608 (1943) and *Continental Ill N B & T Co v Chicago R I & P R Co*, 294 US 648 (1935).

The former was a Chapter X case but the principle decided applies here. This Court said (318 US 618):

"It is urged that a plan of liquidation may constitute a reorganization under Chapter X, and decisions

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69 "Sections 35, 43, and 50 of the bill make similar changes in sections 366, 472 and 656a of the act. These sections presently require a finding that a proposed plan under chapters XI, XII, and XIII shall be 'fair and equitable.' In fact, however, the fair and equitable rule, as interpreted in *Northern Pacific Railway Co. v. Boyd*, 228 U. S. 482, 33 S. Ct. 554, 57 L. Ed. 931 (1913) and *Case v. Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106, 41 Am. B. R. (N. S.) 110, 60 S. Ct. 1, 84 L. Ed. 110 (1939), cannot realistically be applied in a chapter XI, XII, or XIII proceeding. Were it so applied, no individual debtor and, under chapter XI, no corporate debtor where the stock ownership is substantially identical with management could effectuate an arrangement except by payment of the claims of all creditors in full.

"Chapter XI has replaced the old composition procedure under former section 12 of the Bankruptcy Act, where the fair and equitable rule did not apply. Nor is it practicable or realistic to apply the rule in a proceeding under chapter XI, XII, or XIII.

"The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the *Boyd* and *Los Angeles* cases shall not be operative under those 'three chapters.'" Senate Report No. 1395 and House Report No. 2320, 82nd Congress, 2nd Session, paragraph No. 43 in each report.

are cited to that point, but an examination of them will demonstrate that in none save where the corporate purpose of the debtor was, in effect, holding and liquidating securities was the plan such as is proposed here. Under the facts of this case, the suggested plan is but an alternative for ordinary bankruptcy ***."

The latter was a §77 case. It was there said that "a proceeding under §77 is not an ordinary proceeding in bankruptcy" but "is a special proceeding which seeks only to bring about a reorganization."

It is utter nonsense to assert that a "forced merger" will or can safeguard the rights of equitable owners to the extent of the value of their security. Such a claim ignores the mechanics by which a "forced merger" must be produced; the considerations making it desirable to the covetous mergor but rightly objectionable to the mergee; and an ignorance of men and affairs consistent only with an anchorite's detached cogitations.

The key to the "forced merger's" necessary invasion of the mortgagee's property rights is that fundamentally the acquiring railroad dictates the terms of acquisition. The acquiring railroad being an outsider, or at best a member of an inferior unsecured creditor class, cannot be compelled by Court or Commission to acquire the debtor's property. Unless the Commission fixes bargain terms, the acquiring railroad can and will refuse to acquire.

The result cannot be whitewashed with a semantic juggling of the word "value," using terms correctly applied by this Court only to cases involving allocations or allotments among creditors—such as "equitable equivalence." The rule of full and absolute priority is not a rule of "equitable equivalence." It is a rule which enforces the legal and constitutional rights of the prior lien creditor.

The doctrine of "equitable equivalence" applies only to a creditor reorganization in which indebtedness is scaled down to bring it within ability to pay and new securities representing that ability are distributed to creditors in the order of their priority. It is a doctrine which applies only where there are overlapping and conflicting liens, and in marshalling it is necessary to give each lien its relative position in the reorganized debtor. It is not a doctrine which permits squeezing out a senior lien in the fashion here proposed. *Preble Corp v Wentworth*, 84 F 2d 73, 74 (CA 1, 1936) holding that "to take the property from the mortgagee upon an appraisal is an attempt to use a supposed or possible value, over and above the appraisal, for the benefit of other creditors and stockholders. If there is any such surplus value, it belongs to the first mortgagee, up to the amount of his debt."

The evil is not only that of the instant case—it is inherent in the "forced merger" process. This evil of acquisitor-Commission collaboration cuts as deeply as that of the bondholder-stockholder collaboration in the equity receivership cases, of which this Court said in the Boyd case (228 US 507):

> "The invalidity of the sale flowed from the character of the reorganization agreement regardless of the value of the property, for in cases like this, the question must be decided according to a fixed principle, not leaving the rights of the creditors to depend upon the balancing of evidences as to whether, on the day of the sale the property was insufficient to pay prior encumbrances."

CONCLUSION

On the basis of the facts and applicable law, petitioners urge that the judgment of the Court of Appeals should be reversed with directions to that Court to affirm Judge

Strum's order disapproving the so-called "forced merger" fourth plan of reorganization, or that the judgment of the Court of Appeals should be vacated and Judge Strum's order reinstated.

Respectfully submitted,

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APPENDIX A

Section 77 was added to the Bankruptcy Act by the Act of March 3, 1933, 47 Stat 1474, c 204. It was revised by the Act of August 27, 1935, 49 Stat 911, c 774. The controlling provisions, as enacted originally and as revised, are quoted below:

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"(b) A plan of reorganization within the meaning of this section (1) shall include a proposal to modify or alter the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include, in addition, provisions modifying or altering the rights of stockholders generally, or of any class of them; (3) shall provide adequate means for the execution of the plan, which may, *so far as may be consistent with the provisions of sections 1 and 5 of the Interstate Commerce Act as amended,* include the transfer or conveyance of all or any part of the property of the debtor to another corporation or to other

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"(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; *** (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, *** the sale of all or any part of the property of the debtor either subject to or free from any lien at not less than a fair upset price,

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corporations or the consolidation of the properties of the debtor with those of another railroad corporation, or the merger of the debtor with any other railroad corporation ***." (Emphasis supplied)	the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein ***."
"(d) *** Following such hearing, the commission shall render a report in which it shall recommend a plan of reorganization (which may be different from any which has been proposed) that will, in its opinion be equitable, will not discriminate unfairly in favor of any class of creditors or stockholders, will be financially advisable, will meet with the requirements of subdivision (g) of this section, and will be compatible with the public interest. *** Thereafter the plan of reorganization recommended by the commission shall be submitted in such manner as the commission may direct to the creditors and stockholders of the debtor for acceptance or rejection, together with the	"(d) *** the Commission *** shall *** hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. *** The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of

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report or reports of the commission thereon; and the commission may at the same time afford an opportunity to accept or reject any other plan of reorganization filed as in this subdivision (d) provided."

"(e) A plan of reorganization shall not be finally approved by the commission until it has been accepted in writing and such acceptance has been filed in the proceeding by or on behalf of creditors holding two-thirds in amount of the claims of each class whose claims or interests would be affected by the plan, and by or on behalf of stockholders of the debtor holding two-thirds of the stock of each class: *Provided, however,* That if adequate provision is made in the plan for the protection of the interests, claims and liens of any class of creditors or stockholders in the manner provided in clauses (5) and (6) of subdivision (g), of this section, then the acceptance of the plan by such class of creditors or

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the report and order approving the plan. ***"

"(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice *** hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with

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stockholders shall not be requisite to the approval of the plan: *And provided further*, That the acceptance of stockholders shall not be requisite to the confirmation of the plan if (1) the judge shall have determined (a) that the corporation is insolvent, or (b) that the interests of stockholders will not be adversely affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan, and its stockholders are bound by such acceptance. *** Upon acceptance of the plan in accordance with the provisions of this subdivision (e) the commission may, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, or consolidation or merger of properties, to the extent contemplated by the plan *consistent with the purposes of the Interstate Commerce Act as amended.* ***" (Emphasis supplied)

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the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; *** If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) hereof, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, *** *Provided*, That

submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further*, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially

affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. ***"

"(e) *** The Commission shall certify to the judge the results of such submission. ***"

"(f) If the plan recommended by the commission is accepted as provided in subdivision (e), the commission shall thereupon certify the plan to the court together with its approval thereof and that the same has been so accepted, together with a report of the proceedings before it and its conclusions thereon. If the plan accepted as provided in subdivision (e) differs from the plan recommended by the commission it shall, upon acceptance, be submitted to the commission, which shall hear all interested parties upon such notice and subject to such rules and regulations as it shall prescribe. If after such hearing the commission determines that the accepted plan

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in its opinion is equitable and will not discriminate unfairly in favor of any class of creditors or stockholders; will be financially advisable; will meet the requirements of subdivision (g) of this section; and will be compatible with the public interest: the commission shall thereupon certify the plan to the court, together with its approval thereof and that the same has been duly accepted, and together with a report of the proceedings before it and its findings and conclusions thereon. ***"	
"(g) Upon such approval by the commission, and after hearing such objections as may be made to the approved plan, the judge shall confirm the plan if satisfied that (1) the approved plan complies with the provisions of subdivision (b) of this section, is equitable and does not discriminate unfairly in favor of any class of creditors or stockholders; *** (5) the approved plan provides, with respect to stockholders of any class the acceptance	"(e) *** Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is

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of which is requisite to the confirmation of the plan, and who would not become bound by the plan under the provision of subdivision (h) of this section, and of which more than one-third have not accepted the plan, adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan either by a sale of the property at not less than a fair upset price, or by appraisal and payment in cash either of the value of their stock or, at the objecting stockholder's election, of the value of the securities, if any allotted to such stock under the plan; (6) the plan provides with respect to any class of creditors the acceptance of which is requisite to the confirmation of the plan, and who would not become bound by the plan under the provisions of subdivision (h) of this section, adequate protection for the realization by them of the value of their securities, liens, and claims,

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required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided*, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e). *** If it shall be necessary to determine the value of any property for any purpose under this section, the Com-

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either (a) by the sale of such property subject to their liens, if any, or (b) by the sale free of such liens at not less than a fair upset price, and the transfer of such liens to the proceeds of such sale, or (c) by appraisal and payment in cash of either the value of such liens and claims or, at the objecting creditors' election, the value of the securities allotted to such liens and claims under the plan. Section 57, clause (h), of this Act shall be applicable to the appraisal of securities under this section, and the value of the unpaid balance shall be appraised as an unsecured claim; and (7) the debtor, and every other corporation issuing securities or acquiring property under the plan, is authorized by its charter or by applicable State or Federal laws, upon confirmation of the plan, to carry out the plan. In the case of a sale or appraisal under clause (5) or (6) of this subdivision (g) the court shall refer to the com-

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mission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

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mission for its consideration and determination the amount to be fixed as the upset price and the appraisal of any securities."

"(h) Upon such confirmation the provisions of the plan shall be binding upon (1) the corporation, (2) all stockholders if the judge shall have determined (a) that the corporation is insolvent, or (b) that the interests of stockholders will not be adversely affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance, (3) all stockholders of each class of which two-thirds in amount shall have accepted the plan, (4) all creditors whose claims are payable in cash in full under the plan, (5) all creditors entitled to priority under subdivision (c) of this section, whose claims are not payable in cash in full under the plan, provided two-thirds in amount of such creditors shall have accepted the plan

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"(f) Upon confirmation by the judge, the provisions of the plan and of the order of confirmation shall, subject to the right of judicial review, be binding upon the debtor, all stockholders thereof, including those who have not, as well as those who have, accepted it, and all creditors secured or unsecured, whether or not adversely affected by the plan, and whether or not their claims shall have been filed, and, if filed, whether or not approved, including creditors who have not, as well as those who have, accepted it. Upon confirmation of the plan, the debtor and any other corporation or corporations organized or to be organized for the purpose of carrying out the plan, shall have full power and authority to, and shall put into effect and carry out the plan and the orders of the

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in writing filed in the proceeding, (6) all other unsecured creditors, provided two-thirds in amount of such creditors shall have accepted the plan in writing filed in the proceeding, and (7) all secured creditors of each class of which two-thirds in amount shall have accepted the plan. *** Upon confirmation of the plan by the judge, the debtor *and other corporations affected by the plan*, or organized or to be organized for the purpose of carrying out the plan, shall, subject to the jurisdiction of the Commission, have full power and authority to put into effect and carry out the plan and the orders of the judge relative thereto ***." (Emphasis supplied)

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judge relative thereto, under and subject to the supervision and the control of the judge ***. Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation or merger of the debtor's property, or pooling of traffic, to the extent contemplated by the plan *and not inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended.* ***" (Emphasis supplied)

APPENDIX B

Section 5 of Interstate Commerce Act, as enacted by Transportation Act of 1920, Act of February 28, 1920, 41 Stat 456, c 91, codified in 49 USCA §5.

"§5. *Combinations and consolidations of carriers.* ***

"(4) *Consolidation of railroads into limited number of systems.* The commission shall as soon as practicable prepare and adopt a plan for the consolidation of the railway properties of the continental United States into a limited number of systems. In the division of such railways into such systems under such plan, competition shall be preserved as fully as possible and wherever practicable the existing routes and channels of trade and commerce shall be maintained. Subject to the foregoing requirements, the several systems shall be so arranged that the cost of transportation as between competitive systems and as related to the values of the properties through which the service is rendered shall be the same, so far as practicable, so that these systems can employ uniform rates in the movement of competitive traffic and under efficient management earn substantially the same rate of return upon the value of their respective railway properties.

"(5) *Tentative plan of consolidation; hearings; adoption and publication.* When the commission has agreed upon a tentative plan, it shall give the same due publicity and upon reasonable notice, including notice to the governor of each State, shall hear all persons who may file or present objections thereto. The commission is authorized to prescribe a procedure for such hearings and to fix a time for bringing them to a close. After the hearings are at an end, the commission shall adopt a plan for such consolidation and publish the same; but it may at any time thereafter, upon its own motion or upon

application, reopen the subject for such changes or modifications as in its judgment will promote the public interest. The consolidations herein provided for shall be in harmony with such plan.

"(6) *Consolidation of railroads by agreement.* It shall be lawful for two or more carriers by railroad, subject to this chapter, to consolidate their properties or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership, management, and operation, under the following conditions:

"(a) *The proposed consolidation must be in harmony with and in furtherance of the complete plan of consolidation mentioned in paragraph (5)* and must be approved by the commission; *** (Emphasis supplied)

"(c) Whenever two or more carriers propose a consolidation under this section, they shall present their application therefor to the commission, and thereupon the commission shall notify the governor of each State in which any part of the properties sought to be consolidated is situated and the carriers involved in the proposed consolidation, of the time and place for a public hearing. If after such hearing the commission finds that the public interest will be promoted by the consolidation and that the conditions of this section have been or will be fulfilled, it may enter an order approving and authorizing such consolidation, with such modifications and upon such terms and conditions as it may prescribe, and thereupon such consolidation may be effected, in accordance with such order, *if all the carriers involved assent thereto*, the law of any State or the decision or order of any State authority to the contrary notwithstanding. (Emphasis supplied)

APPENDIX C

Section 5 of Interstate Commerce Act, as amended by Transportation Act of 1940, Act of September 18, 1940, 54 Stat 898, c 722, codified in 49 USCA §5, pocket part supplement.

"§5. *Combinations and consolidations of carriers—Pooling; division of traffic service, or earnings* ***

"*Unifications, mergers, and acquisitions of control*

"(2) (a) It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision (b)—

"(i) for two or more carriers to consolidate or merge their properties or franchises, or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership; or for any carrier, or two or more carriers jointly, to purchase, lease, or contract to operate the properties, or any part thereof, of another; or for any carrier, or two or more carriers jointly, to acquire control of another through ownership of its stock or otherwise; or for a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise; or

"(ii) for a carrier by railroad to acquire trackage rights over, or joint ownership in or joint use of, any railroad line or lines owned or operated by any other such carrier, and terminals incidental thereto.

"(b) Whenever a transaction is proposed under subparagraph (a), the carrier or carriers or person seeking authority therefor shall present an application to the Commission, and thereupon the Commission shall notify the Governor of each State in which any part of the properties of the carriers involved in the proposed transaction is situated, and also such carriers and the applicant or applicants (and, in case carriers by motor vehicle are involved, the persons specified in section 305 (e)), and shall afford reasonable opportunity for interested parties to be heard. If the Commission shall consider it necessary in order to determine whether the findings specified below may properly be made, it shall set said application for public hearing; and a public hearing shall be held in all cases where carriers by railroad are involved unless the Commission determines that a public hearing is not necessary in the public interest. If the Commission finds that, subject to such terms and conditions and such modifications as it shall find to be just and reasonable, the proposed transaction is within the scope of subparagraph (a) and will be consistent with the public interest, it shall enter an order approving and authorizing such transaction, upon the terms and conditions, and with the modifications, so found to be just and reasonable; Provided, That if a carrier by railroad subject to this chapter, or any person which is controlled by such a carrier, or affiliated therewith within the meaning of paragraph (6), is an applicant in the case of any such proposed transaction involving a motor carrier, the Commission shall not enter such an order unless it finds that the transaction proposed will be consistent with the public interest and will enable such carrier to use service by motor vehicle to public advantage in its operations and will not unduly restrain competition.

"(c) In passing upon any proposed transaction under the provisions of this paragraph (2), the Commission

shall give weight to the following considerations, among others: (1) The effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected.

"(d) The Commission shall have authority in the case of a proposed transaction under this paragraph (2) involving a railroad or railroads, as a prerequisite to its approval of the proposed transaction, to require, upon equitable terms, the inclusion of another railroad or other railroads in the territory involved, upon petition by such railroad or railroads requesting such inclusion, and upon a finding that such inclusion is consistent with the public interest." ***

"Plenary nature of authority under section

"(11) The authority conferred by this section shall be exclusive and plenary, and any carrier or corporation participating in or resulting from any transaction approved by the Commission thereunder, shall have full power (with the assent, in the case of a purchase and sale, a lease, a corporate consolidation, or a corporate merger, of a majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the shares entitled to vote of the capital stock of such corporation at a regular meeting of such stockholders, the notice of such meeting to include such purpose, or at a special meeting thereof called for such purpose) to carry such transaction into effect and to own and operate any properties and exercise any control or franchises acquired through said transaction ***."

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IN THE

Supreme Court of the United States

OCTOBER TERM, ~~1952~~ 1953

No. ~~510~~ 37

IN THE MATTER OF THE FLORIDA EAST COAST RAILWAY CO.,
Debtor,

W. G. WELBON, E. N. CLAUGHTON, and A. W. CORBETT,
Petitioners,

vs.

ATLANTIC COAST LINE RAILROAD CO.,
Respondent.

BRIEF OF THE RESPONDENT, ATLANTIC COAST LINE RAILROAD COMPANY, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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15, 1953

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

No. 710

IN THE MATTER OF THE FLORIDA EAST COAST RAILWAY CO.,
Debtor,

W. G. WELBON, E. N. CLAUGHTON, and A. W. CORBETT,
Petitioners,

vs.

ATLANTIC COAST LINE RAILROAD CO.,
Respondent.

BRIEF OF THE RESPONDENT, ATLANTIC COAST LINE RAILROAD COMPANY, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

This petition relates to the same order of the Court of Appeals, Fifth Circuit, as Nos. 670, 702 and 705.

OPINIONS BELOW.

The opinions of the Courts and the reports and orders of the Interstate Commerce Commission are referred to in the petitioners' brief (p. 14-15). Further detail will be found in the respondent's brief in No. 670 (p. 2-4).

The Record.

The petitioners refer to the six volumes, I to VI, now before this Court in No. 670. They attach to their petition a copy of the opinion of the Court of Appeals on the prior appeal (179 F. 2d 538); a copy of their petition for a rehearing of the Court of Appeals' order reversing Judge

STRUM; and a copy of the order of the Court of Appeals dated March 2, 1953, denying the petition for rehearing.

They make no reference to the unprinted portions of the record which were before the Court of Appeals and are now before this Court in No. 670. However, we assume that the unprinted record will be deemed before this Court in connection with the petition.*

JURISDICTION.

This Court's jurisdiction is invoked under 28 U. S. C. § 1254.

THE QUESTIONS PRESENTED.

The questions presented by the petitioners are referred to later herein under the Argument.

STATUTE INVOLVED.

The statute involved is Section 77 of the Bankruptcy Act (11 U. S. C. § 205). The pertinent portions will be found in Appendix A to the respondent's brief in No. 670.

STATEMENT OF THE CASE.

The petitioners' statement of the case incorporates by reference (p. 16) the portion of the petition which follows the heading "SUMMARY STATEMENT" (p. 1-11).

The object of the petitioners' Summary Statement: the relationship of the Summary Statement to the Questions Presented.

The petitioners' questions presented read almost like pure questions of law, in connection with which an 11-page

* A notice served by the petitioners on counsel for the respondent contains the following paragraph:

> "The petition makes a part thereof by reference the record now before the Court upon petition for certiorari by St. Joe Paper Company et al., No. 670 October Term, 1952, in which you are counsel for the respondent, and prays reference to that record in support of the petition in the instant cause."

This would seem to cover the unprinted portions of the record.

"SUMMARY STATEMENT" would be wholly unnecessary. But in the statement of the questions presented there are suggestions of the theme of the petition and brief (p. 11-12).

That theme is that the Commission and the Court of Appeals have been arbitrary and that the so-called "minority bondholders" of the Florida East Coast will suffer if the Commission's Plan be consummated.

> ***The petitioners repeat the erroneous statement, several times made by Judge Strum and by the petitioners in Nos. 670 and 702, that the Plan is opposed by the holders of more than 99% in amount of the Bonds.***

As we showed in the respondent's brief in No. 670 (p. 10-12), there is no warrant for the petitioners' statement that the Plan was "objected to in the District Court on behalf of holders of more han 99% in amount of the 5% bonds" (p. 9; see also p. 7).

If there had been a good case on the merits against the Commission's Plan, the appellees in the Court of Appeals and the petitioners in this Court would doubtless have scorned to stand on Judge STRUM's finding that the Plan is opposed by holders of 99% in amount of the Bonds. For that finding is demonstrably "without support in law or in fact".*

> ***While professing to speak for the "minority bondholders" generally, the petitioners (like the petitioners in Nos. 670, 702 and 705) make no effort to show that the Court of Appeals was wrong in finding, in effect, that the Commission's Plan is favorable to the bondholders as a class and hence favorable to the minority bondholders.***

In the respondent's brief in No. 670 we quoted the findings of the majority of the Court of Appeals which

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* Not all of the appellees below or all of the petitioners in this Court have tried to stand on Judge STRUM's finding. As we noted in the respondent's memorandum in No. 705, the Successor Mortgage Trustees do not contend that the Plan is opposed by the holders of 99% in amount of the Bonds.

are to the effect that the Plan is not merely fair, but distinctly favorable, to the holders of the First and Refunding Mortgage Bonds as a class (p. 9). Also, in discussing Judge STRUM's findings, and the Judge's disregard of the Commission's fair market value findings and the fair market value evidence in the District Court, we sketched briefly some of the principal features of the overwhelming showing that the Plan is favorable to the bondholders as a class (p. 53-57). The petitioners make no effort to show that the Court of Appeals was wrong. Instead they quote Judge STRUM's statement that the Plan "does not afford due recognition to the rights of the 5% bondholders, *particularly the minority groups* (p. 2; emphasis supplied by the petitioners) and refer to his holding that the "$20,000,000 of minority 5% bondholders" should not "be penalized by the Commission's apprehensions as to the public interest" (petition p. 9-10 footnote; I, 164;* 103 F. Supp. 845). In addition, they quote in a footnote (p. 9) Judge STRUM's reference to "the distinct prejudice of the $20,000,000 of minority 5% bondholders" and his statement that the Plan is particularly unfair to "the minority groups, who are innocent bystanders caught between the upper and neither millstone, and who now, like ancient Odysseus, drift helplessly between Scylla and Charybdis, hoping to be rescued" (I, 141; 103 F. Supp. 835).

The words "penalized" and "distinct prejudice" which Judge STRUM used imply that the Plan is economically disadvantageous to the "$20,000,000 of minority 5% bondholders". But at most Judge STRUM merely expressed an ultimate conclusion. He did not mention the Commission's findings or the evidence. He left the whole subject of the *economic effect of the Plan* severely alone except for repeated statements which were substantially to

* In this and similar citations the Roman numerals refer to the volume of the printed record and the Arabic numbers to the page.

the effect that it made no difference how valuable the cash and securities which the Atlantic Coast Line would provide under the Plan might be (see respondent's brief in No. 670, p. 55-57). He said that it was immaterial if the securities of the Atlantic Coast Line had "an *ostensible value*" equal to that of the present securities of the debtor railroad" and he most distinctly implied that any of the securities of the Atlantic Coast Line, of whatever amount, calibre and market value, would be "unwanted" and unacceptable because they are "of fluctuating and debatable value" (*id.*).

It is unthinkable that, if the various petitioners for certiorari could show by the record that the so-called "minority bondholders" would in fact be penalized under the Commission's Plan, they would have relied in the Court of Appeals, and would rely now, merely on what Judge STRUM said in his opinion.

Yet we now have four petitions and briefs in Nos. 670, 702, 705 and 710 totaling 81 pages, exclusive of appendices, and in all 81 pages there is no effort to show that in fact the Florida East Coast bondholders would be penalized economically under the Plan—no effort to show that the Court of Appeals was wrong in finding that the Plan is fair to all of the bondholders.

While the petitioners compliment Judge STRUM for his "exhaustive" opinion, they criticize Chief Judge HUTCHESON's opinion as containing "dogmatic assertions" and "dogmatic conclusions" (p. 10). We do not know whether the word "dogmatic" is used in an invidious sense; if it is, its use is unwarranted. In this connection it is sufficient to refer to the respondent's brief in No. 702 at pages 6-9.

The Petitioners: The Welbon (Claughton) Group.

The petitioners purport to speak for the "minority bondholders" generally.

Consequently the data about the Welbon (Claughton) Group in Appendix B to the respondent's brief in No. 670 (p. ix-xi) is pertinent. It reveals, among other things, *first*, that the leader of the Group, E. N. Claughton, has been a very heavy and active speculator in the First and Refunding Mortgage Bonds, his holdings having declined from $3,500,000 on December 10, 1948 to $2,000 on July 11, 1950; *second*, that his speculations have been largely financed by loans from the Florida National Bank at Miami, which is controlled by the St. Joe Paper Company; and, *third*, that the other members of the Group have, or have had, loans from one or more of the banks which are members of the Florida National Group of Banks, controlled by St. Joe-duPont.

It would be a travesty to treat the petitioners as spokesmen for the minority bondholders.

ARGUMENT

THE PETITIONERS' REASON 1.

The petitioners' Reason 1 (p. 17-18) involves the first question which was presented by the petitioners in No. 670 (see the respondent's brief in No. 670, p. 25-46).

The petitioners stress the alleged novelty of the question which they say is presented. But in order to be able to say that the question is novel they find it necessary to state the question in such a way as to make an apparent distinction between the Plan in this case and the plan involved in *Old Colony Bondholders* v. *New York, N. H. & H. R. Co.* (C. C. A. 2, 1947) 161 F. 2d 413, cert. den. *Protective Committee for Bonds of Old Colony Railroad Co.* v. *New York, New Haven & Hartford Railroad Co.* (1947) 331 U. S. 858, rehearing denied (1947) 332 U. S. 803, which is referred to in the respondent's brief in No. 670 at page 39. Consequently they refer to the Atlantic Coast Line as "an unaffiliated, wholly unrelated railroad, which is not being reorganized under § 77 or otherwise". But

they do not say what difference it makes that the Atlantic Coast Line is not affiliated with the Florida East Coast or is not being reorganized. And, as has been pointed out in the respondent's brief in No. 670 (p. 38-39), the arguments advanced against the Commission's Plan in this case would, if valid, apply to the plan in the *Old Colony* case.

The petitioners contribute the thought that the words "another corporation or corporations" in Section 77 (b)(5) should be construed to mean "another corporation or corporations *organized or to be organized for the purpose of carrying out the plan* (emphasis supplied by the petitioners) because the italicized words will be found in the second sentence of subsection (f).

It hardly seems necessary to say more than that the italicized words are in Section 77 (f) but not in Section 77 (b)(5). It must be assumed that the Congress put them in Section 77(f) and left them out of Section 77(b)(5) intentionally. As the Commission said (267 I. C. C. 730), if the Congress had intended to restrict the broad provision of Section 77(b)(5), "the assumption is that it would have added the necessary language to make effective that restriction".

The petitioners' argument (p. 18) that the provision of Section 77(b)(5) was "merely intended to preserve and authorize the established equity device of organizing a corporation or corporations as a means for the execution of a plan" is refuted by the explicit language of Section 77(b)(5), which refers not only to a transfer but also to a "merger or consolidation". The "established equity device" did not involve either a merger or a consolidation—it involved a sale to a new corporation organized to carry out a plan. So far as we know, there has *never* been a case in equity (or, for that matter, in Section 77) in which a new corporation was formed and then the debtor was merged into or consolidated with the new corporation. There can be no doubt that when the Congress adopted the language

of Section 77(b)(5) it had in mind much more than the "established equity device".

Section 77(b)(5) relates to what a plan can do. The second sentence of Section 77(f), on which the petitioners rely, contains a grant of power to execute a plan. The petitioners make no effort to show that it is not entirely logical to have different provisions in the two subsections.*

If the words in the second sentence of Section 77(f) could be deemed to restrict the provisions of Section 77(b)(5), then the plan of reorganization of the Alton, under which the Alton was transferred to the Gulf, Mobile & Ohio, was wholly unauthorized. *Alton Railroad Company Reorganization* (1945) 261 I. C. C. 343. And it is interesting to note that on March 27, 1953, in *New Jersey & New York Railroad Company Reorganization*, Finance Docket 13490, the Commission (by Division 4) approved a plan for the reorganization of The New Jersey and New York Railroad Company under which the debtor's properties would be transferred to Erie Railroad Company; if the petitioners' contention were sound, that plan too would be unauthorized.

THE PETITIONERS' REASON 2.

The petitioners' Reason 2 is stated as follows (p. 18-19):

> "The Court of Appeals so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. The departures were: First, the failure of the Court of Appeals to decide petitioners' contention that § 77 of the Bankruptcy Act,

* There would seem to be much stronger reason for uncertainty as to the effect of the second sentence of Section 77(f) than for doubt as to the effect of Section 77(b)(5). Actually the practice has been for reorganization managers, rather than debtors, to carry out plans pursuant to court orders. The provision of the Plan in this case, that the reorganization managers "shall carry out the plan under the supervision and control of the court" (282 I. C. C. 225), is the conventional one under which many Section 77 plans have been carried out, frequently over the active opposition of debtors.

as construed, violates the due process and eminent domain clauses in the Fifth Amendment; second, the failure of the Court of Appeals to give any consideration to the rights and equities of the minority bondholders, as distinguished from those of the majority bondholder."

The Alleged Constitutional Question.

Prior to this Court's decision in *Reconstruction Finance Corporation* v. *Denver & Rio Grande Western Railroad Co.* (1946) 328 U. S. 495 it was vigorously argued that *Louisville Joint Stock Land Bank* v. *Radford* (1935) 295 U. S. 555 established that the bondholders had a constitutional right to a foreclosure sale.*

The *Denver & Rio Grande* decision effectively disposed of any argument that a plan such as the present Plan would be unconstitutional. This Court said (328 U. S. p. 533):

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* The argument made by the St. Joe Paper Company was summarized in the Commission's Third Supplemental Report, dated April 8, 1947, as follows (267 I. C. C. 303, footnote omitted):

> "The St. Joe Paper Company contends that, in the absence of full payment of the first and refunding bondholders' claim or of a public sale of the debtor's properties at an upset price fixed by us, these bondholders are entitled upon reorganization to possession of all the properties of the debtor including its cash on hand. It further asserts that any interpretation of the powers conferred upon us and the court by section 77 which would permit of a denial of this right to the bondholders over their objection (and in the absence of an exercise of the right of eminent domain) would violate the fifth amendment of the Constitution. The St. Joe Company bases its argument fundamentally on the decision of the United States Supreme Court in *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555."

The *Denver & Rio Grande* case was decided on June 10, 1946. While the Third Supplemental Report was issued later and refers to the *Denver & Rio Grande* decision (267 I. C. C. 304), the paragraph from the Report which we have quoted summarizes the contention pressed by the St. Joe Paper Company in its brief filed in February, 1946, after the November, 1945, hearings and before the *Denver & Rio Grande* opinion was issued.

"We think that the provisions for confirmation by the courts over the creditors' objection are within the bankruptcy powers of Congress. Those powers are adequate to eliminate claims by administrative valuations with judicial review and they are adequate to require creditors to acquiesce in a fair adjustment of their claims, so long as the creditor gets all the value of his lien and his share of any free assets.[26]

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[26] *Wright* v. *Union Central Ins. Co.*, 311 U. S. at 278, and discusion at p. 509, *supra*.

After *Denver & Rio Grande* had been decided, the references in this case to any possible constitutional question became more in the nature of hints that there might be a question than arguments that a plan such as the present Plan would involve a violation of the Fifth Amendment (see, for example, the petition in No. 670 at p. 26).

Judge SIBLEY said that his conclusion made it "unnecessary to determine whether the Court's power in bankruptcy could be extended to force a merger consistently with the Fifth Amendment" (V, 476; 81 F. Supp. 932). Judge RUSSELL used identical language except that he said that there was "a serious constitutional question" (II, 732-733; 201 F. 2d 331).

In both opinions as well as in the petitioners' brief the sole constitutional power mentioned is the bankruptcy power. There is no mention of the interstate commerce power. If there were any real doubt that the bankruptcy power is broad enough to cover authority for a "forced merger", it would be suitable to consider the scope of the interstate commerce power. Compare *North American Company* v. *Securities and Exchange Commission* (1946) 327 U. S. 686, 709-710.

However, this Court's holding in *Denver & Rio Grande*, following the decision in *Wright* v. *Union Central Life Insurance Company* (1940) 311 U. S. 273, left no doubt as to the extent of the bankruptcy power, even if that were to be

taken by itself. After the *Denver & Rio Grande* decision a transfer of mortgaged property was made, over the objection of a majority in amount (of those voting) of the mortgage bondholders, in each of two cases: *In re Chicago, R. I. & P. Ry. Co.* (C. C. A. 7, 1947) 160 F. 2d 942; cert. den. *Chase National Bank, Trustee* v. *Cheston* (1947) 332 U. S. 793, rehearing denied (1947) 332 U. S. 826 and *Old Colony Bondholders* v. *New York, N. H. & H. R. Co.* (C. C. A. 2, 1947), 161 F. 2d 413, cert. den. *Protective Committee for Bonds of Old Colony Railroad Co.* v. *New York, New Haven & Hartford Railroad Co.* (1947), 331 U. S. 858, rehearing denied (1947) 332 U. S. 803. If there were any constitutional bar to the Commission's Plan, then the same bar would have stood in the way of the transfer of the property subject to the Little Rock and Hot Springs Western First Mortgage in the reorganization of the Rock Island and the transfer of the property subject to the Old Colony Railroad First Mortgage in the reorganization of the New Haven. For, even if on a question of statutory construction a distinction could be made that the Atlantic Coast Line Railroad Company is "an unaffiliated, wholly unrelated railroad", no such distinction could have any significance in determining the constitutional power of the Congress.

* * * *

The petitioners refer (p. 20) to "the proposed taking of their property by Coast Line, at a price which has never been determined to be its present fair value, for compensation which is not payable in cash".

We are at a loss to know the meaning of their statement that the "price" has never been determined to represent the "present fair value" of the property, particularly in view of the findings of the Court of Appeals.

With respect to the complaint that the compensation is not payable in cash, any contention that bondholders in a railroad reorganization can insist on cash—that is, on dollars rather than on securities—has been an anachronism

since this Court's decisions in the *Western Pacific*, *Milwaukee* and *Denver & Rio Grande* cases. In this connection it is sufficient to refer to the parts of the *Western Pacific* and *Milwaukee* opinions which are cited in the footnote at page 13 of the respondent's brief in No. 702. It is unnecessary to add that the Florida East Coast bondholders fare better under the Commission's Plan, which provides for Atlantic Coast Line securities, than they would under a plan providing for a payment only in dollars—dollars have fluctuated downward in terms of what dollars will buy since the Commission approved the Plan in 1951, whereas Atlantic Coast Line securities, particularly Atlantic Coast Line Common Stock, have fluctuated upward in terms of dollars.*

The alleged failure of the Court of Appeals to consider the rights of the minority bondholders.

The petitioners really argue two propositions.

First, they say (p. 21) that the Court of Appeals disregarded Judge STRUM's holding that the Plan "unjustly and inequitably subordinates the rights of the 5% bondholders, *particularly the $20,000,000 of minority bonds*" (emphasis supplied by petitioners). That proposition has been discussed above at pages 3-5.

If, as the Court of Appeals found, the Plan is favorable to the bondholders as a class, how can it be unfair to the so-called minority? And how can it be said that the Court of Appeals disregarded the rights of a minority of a class,

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* The Commission found the fair market value of the securities which would be issued under the Plan based on the level of security prices prevailing on May 25, 1951 (282 I. C. C. 157, 162-163). The market value of the Atlantic Coast Line Railroad Company Common Stock at that time was 64. The price put by the Commission on the Participating Cumulative Convertible Preferred Stock was 70; that stock, being convertible into Common Stock, would be bound to sell at a price at least as high of the Common Stock. At the present time the market price of the Common Stock is well over 100 and the Participating Cumulative Convertible Preferred Stock would also sell at over 100.

when the Court made explicit findings that the Plan is fair, if not generous, to the whole class?

Second, the petitioners suggest that Judge STRUM had a discretionary power which the Court of Appeals ignored (p. 21-22). The Lynch Interests made a similar suggestion in No. 702 and we refer to the respondent's brief therein (p. 4-11).

THE PETITIONERS' REASON 3.

The petitioners' Reason 3 seems to be a consolidation of Reasons 1 and 2, with the addition of an assertion that the questions presented are of "paramount importance" and a contention that the "stated purpose of the plan is to preclude realizing the highest possible sale price for the bondholders' security" (p. 23).

In support of the latter extraordinary contention the petitioners quote a statement made by the Commission, in its Third Supplemental Report in 1947, in support of its refusal to direct a foreclosure in connection with the Previous Plan (p. 22). The gist of the Commission's 1947 statement was that, if there were a judicial sale, "the Coast Line obviously could not successfully compete in bidding with the debtor's first and refunding bondholders". It is immaterial whether or not the Commission was correct in making this statement in 1947, as it does not appear that either the statement, or any thought that lay behind the statement, influenced what the Commission did in 1951.

Moreover, the petitioners' effort to make something of the Commission's statement compels them to rely on the mistaken hypothesis that a judicial sale would result in a higher "price" than the Commission's Plan provides and that the result of the Commission's failure to provide for a judicial sale "is to preclude realizing the highest possible sale price for the bondholders' security and to limit the sale price to so-called reorganization value expressed in terms of Coast Line securities" (p. 23).

This superficially plausible hypothesis can be tested in the light of experience with foreclosure sales of railroads.

When at the instance of the petitioners Judge STRAUM directed the dismissal of the proceeding, he said that one of the purposes was to "enable the Atlantic Coast Line, the 5% bondholders, the employees, and any other interested persons, to bid for the property at a public, competitive sale" (I, 167; 103 F. Supp. 847). But in more than 50 years there apparently has never been a single instance of a true "public, competitive sale" of a railroad. *Weiner, Conflicting Functions of the Upset Price in a Corporate Reorganization*, 27 Col. L. Rev., 132, 137 (footnote 28); *Dewing, The Financial Policy of Corporations*, The Ronald Press Company, Revised Edition, p. 964.

There is no reason to suppose that, if there were an attempt in this case to have a "public, competitive sale", there would be more than two possible bidders: (1) a corporation controlled by the St. Joe Paper Company and (2) the Atlantic Coast Line Railroad Company. If either were eliminated by a failure to get Interstate Commerce Commission authority or because of the difficulty of financing the cash requirements of the purchase, the other would be left as the sole potential bidder and the so-called "minority bondholders", for whom these petitioners purport to speak, would be left pretty much at the mercy of the sole bidder.*

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* We argued before Judge STRAUM that any corporation controlled by the St. Joe Paper Company would be eliminated from the bidding because it would need Commission authority under Section 5(2) of the Interstate Commerce Act to acquire the Debtor's property, *Minneapolis & St. Louis Railroad Company Reorganization* (1941) 244 I. C. C., 357, 360, and that in view of the Commission's decisions in this case it was necessary to presume that the Commission would deny such authority. Judge STRAUM did not pass on the point.

Presumably what the Commission said in its 1947 report was the result of an assumption that it would be difficult for the Atlantic Coast Line to make a *cash* bid for the Florida East Coast, while the cash requirements which the St. Joe Paper Company would have to meet would be greatly reduced because of its bondholdings. A principal difficulty about making a *cash* bid would involve the time factor. It is difficult to see how it would be possible to avoid an underwriting commitment which would run for a substantial period of time and involve heavy expense if obtainable at all.

There is simply no basis for the assumption that the "minority bondholders" would be better off if there were a "public, competitive sale". They would run a real risk of being very much worse off.

The real protection which holders of railroad securities have in railroad reorganizations, whether in Section 77 or in equity, consists of the legal requirements for determinations of fairness, whether by the Interstate Commerce Commission or by the Court. A judicial sale is a mere device.

As long ago as in 1922, in *Reorganization—The Next Step*, 22 Col. L. Rev. 14, James N. Rosenberg accurately and colorfully described the function of a foreclosure sale while urging a change in the equity practice much along the line later followed by the Congress when it enacted Section 77. In discussing the suggested change he said (p. 26):

> "What then becomes of that sacrosanct proceeding, the foreclosure which takes place so frequently as a part of reorganization? Sacrosanct? It is a matter of practice merely. If a sale is but a 'step in reorganization,' why not bury the foreclosure among the ancient relics of outworn practice? Why not a sale free of liens as in bankruptcy practice? The safeguards of foreclosure were not intended for the benefit of creditors, but for the protection of the holder of the equity of redemption. Forward-looking lawyers have torn down many exacting structures of technique. Traver, writs of disseizin, enfeoffment, confession and avoidance, rejoinder and surrejoinder—the very words are strange to the modern lawyer's ears. As technique in art is but the servant of beauty, so technique, practice, procedure in the law are but the handmaids of Justice—otherwise the law becomes a vain and empty ritual."

THE PETITIONERS' REASON 4.

The petitioners' Reason 4 (p. 24-25) relates to the absolute priority rule and in connection with it we refer to the respondent's brief in No. 702 (p. 11-15).

The key word which is quoted and used by the petitioners is "receive". They quote parts of sentences from the *Denver and Rio Grande* and *Western Pacific* opinions which use the word "receive". They then speak of what the Atlantic Coast Line will "receive".

If the quotations from the *Denver and Rio Grande* and *Western Pacific* opinions be read in context, it will be immediately apparent that they relate to the distribution among several classes of creditors, which have claims against a particular property, of what is received for that property under a plan. In other words, in both instances this Court was enunciating the absolute priority rule *as a rule of distribution*, and that, of course, is what it is.

In this case there is no issue which involves any question of distribution. What is received under the Plan for the mortgaged properties goes to the mortgagees and, since the First Mortgage will be paid off, all of it goes to the holders of the First and Refunding Mortgage Bonds. What is received for the unmortgaged assets goes to the unsecured creditors (including the secured creditors to the extent that they are entitled to be treated as unsecured creditors).

As a junior creditor the Atlantic Coast Line will not receive anything except in respect of the unmortgaged assets.

The petitioners say that "the junior claim will receive all of debtor's property" (p. 25). It is true that the Atlantic Coast Line will acquire all of the Debtor's property. It is also true that it is the holder of a junior claim. But it is not correct to say that "the junior claim will receive all of debtor's property". For whatever properties are

transferred to the Atlantic Coast Line, it will provide a consideration, in cash and securities, which has been determined to be the equivalent of what will be transferred to it.

CONCLUSION.

The petition should be denied.

Dated, April 15, 1953

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1953

No. 37

IN THE MATTER OF FLORIDA EAST COAST RAILWAY COMPANY,
Debtor,

W. G. WELBON, E. N. CLAUGHTON and A. W. CORBETT,
Petitioners,

VS.

ATLANTIC COAST LINE RAILROAD CO.,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF THE RESPONDENT, ATLANTIC COAST LINE RAILROAD COMPANY

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IN THE

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No. 37

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vs.

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Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT.

BRIEF OF THE RESPONDENT, ATLANTIC COAST LINE RAILROAD COMPANY

This Court granted a writ of certiorari herein limited to Question I presented by the petition for the writ in No. 670, now No. 24 (345 U. S. 948), which is quoted at pages 4-5 of the petitioners' brief herein and at pages 4-5 below.

The writ relates to an order of the Court of Appeals, Fifth Circuit, sitting *en banc*, entered on January 19, 1953, by which that Court (Chief Judge HUTCHESON, Judges HOLMES and RIVES, with Judges RUSSELL and BORAH dissenting) reversed an order dated March 11, 1952 of the District Court for the Southern District of Florida (Circuit Judge STRUM sitting as a District Judge) and directed the

District Court to approve a plan of reorganization of the Debtor, which the Interstate Commerce Commission had approved and certified to the District Court pursuant to Section 77 of the Bankruptcy Act.

The plan, referred to herein as "the Commission's Plan" or simply as "the Plan", provides that the properties of the Debtor (with certain exceptions) shall be transferred to Atlantic Coast Line Railroad Company by a merger or consolidation of the two corporations or a transfer and conveyance by the Debtor's Trustees, and that the Atlantic Coast Line shall turn over cash and Atlantic Coast Line securities (two classes of bonds and two classes of stock) to be distributed among the creditors of the Debtor.

OPINIONS BELOW.

The opinion of the Court of Appeals (II, 717-733[1]) is reported: *In re Florida East Coast Ry. Co.*, 201 F. 2d 325. The opinion in the District Court (I, 127-168) is reported: *In re Florida East Coast Ry. Co.*, 103 F. Supp. 825.

The Commission approved the Plan initially in its Fifth Supplemental Report of July 12, 1951, *Florida East Coast Railway Company Reorganization*, 282 I. C. C. 81-191, and the Commission modified the Plan slightly, and approved it as modified, in its Sixth Supplemental Report of October 25, 1951, and its Order of the same date, *Florida East Coast Railway Company Reorganization*, 282 I. C. C. 195-226. Photo-lithographed copies of the Fifth and Sixth Supplemental Reports and the Order of October 25, 1951 will be found consecutively at the front of Volume I of the Record. The definitive Plan will be found in the Order (282 I. C. C. 213-226).

* * * * *

An earlier plan, providing for a unification of the Debtor with the Atlantic Coast Line, which was approved

[1] In this and similar citations the Roman numerals refer to the volume of the printed record and the Arabic numbers to the page.

in the Commission's Third and Fourth Supplemental Reports, *Florida East Coast Railway Company Reorganization*, 267 I. C. C. 295-391, 267 I. C. C. 729-759,[1] was the subject of an opinion in the District Court (Circuit Judge SIBLEY), *In re Florida East Coast Ry. Co.*, 81 F. Supp. 926, and an appeal, *Atlantic Coast Line R. Co.* v. *St. Joe Paper Co.*, 179 F. 2d 538. Atlantic Coast Line Railroad Company, respondent now, petitioned for certiorari, which was denied, *Atlantic Coast Line Railroad Co.* v. *St. Joe Paper Co.*, 339 U. S. 929.[2]

The Record.

The printed record consists of six Volumes. Nos. I-III comprise the printed record on appeal in the Court of Appeals, with the proceedings in the Court of Appeals at the back of Volume II. Nos. IV-VI comprise the printed record in the Court of Appeals on the prior appeal.

The unprinted record consists of everything which was before the Court of Appeals in unprinted form. It contains everything in the Atlantic Coast Line's Designation of Contents of Record (I, 173-229) which is not in any of Volumes I-VI.

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[1] Photo-lithographed copies of these two Reports will be found in Volume IV of the Record, immediately following a photo-lithographed copy of the Second Supplemental Report.

[2] The Commission first approved a plan on April 6, 1942, *Florida East Coast Railway Company Reorganization*, 252 I. C. C. 423 (VI, 528-640). After consideration of petitions for modifications the plan was modified in certain respects and approved as modified in the Commission's Supplemental Report of August 10, 1942, *Florida East Coast Railway Company Reorganization*, 252 I. C. C. 731 (VI, 641-689). On October 19, 1943 District Judge STRUM sustained objections to the plan and remanded it to the Commission, *In re Florida East Coast Ry. Co.*, 52 F. Supp. 420 (VI, 690-697). After hearings the Commission approved a plan for an "internal reorganization" on January 8, 1945 in its Second Supplemental Report, *Florida East Coast Railway Company Reorganization*, 261 I. C. C. 151-193. (A photo-lithographed copy of the Second Supplemental Report will be found at the front of Volume IV of the record.) After the filing of various petitions for modifications, some of which contained requests for further hearing, the Commission reopened the case (267 I. C. C. 295-296).

JURISDICTION.

The writ was granted under 28 U. S. C. § 1254.

THE QUESTION PRESENTED.

The petitioners' brief quotes correctly (p. 4-5) the statement of the Question Presented as the question was put in the petition for a writ in No. 670 (now No. 24):

"It being clear that Section 77 of the Bankruptcy Act, as enacted in 1933, did not authorize the Interstate Commerce Commission to prevent a plan of reorganization of a railroad involving a 'forced' merger of the debtor Railway with another railroad, the question is whether amendments to the 1933 Act, made in 1935, do authorize forced mergers.

The Act of 1933 for railroad reorganizations in bankruptcy contained in subdivision (b) a so called consistency clause which qualified the powers of the Commission in respect of mergers, by expressly providing that a merger would have to be brought about by compliance with *'provisions'* of the Interstate Commerce Act which allowed mergers *only* if requested and agreed to by the carrier and then approved by the Commission, after notice to the Governors of the states, and after hearing communities and shippers served by the carriers. This 'consistency' provision in this legislation was repeated in subd. (e) of the 1933 Act, where it was said that transfers of property or consolidations or mergers may be made 'to the extent contemplated by the plan *consistent with the purposes* of the Interstate Commerce Act as amended'. It will be noted that the clause in (b) used the word 'provisions' and the clause in (e) used the word 'purposes'. By amendments in 1935 these two 'consistency' clauses were consolidated and transplanted from (b) and (e) to subdivision (f).

In the 1935 Act, subd. (f), the clause allowing

transfer and mergers had the qualification 'to the extent contemplated by the plan' and 'not inconsistent with the provisions and purposes of Chapter 1 of Title 49 as on August 27, 1935 or thereafter amended.'

The narrow question is therefore whether the mere transfer of the 'consistency' clauses from subdivisions (b) and (e) of subdivision (f) altered the meaning of the clauses and gave to the Interstate Commerce Commission a power to force mergers, which was withheld from it under the Act of 1933."

When we say that the petitioners have correctly quoted the question presented as the question was put in the petition for a writ in No. 670 (now No. 24), we do not mean that we concede the correctness of what is said or implied in the statement of the question presented. The extent to which we differ will appear later herein as well as in our brief in No. 24.

The Petitioners' disregard of the limitation in this Court's order granting certiorari.

These petitioners filed a petition for certiorari, No. 710, in which they listed six questions on which they wished to have this Court pass (p. 11-13). The first was to some extent similar to Question I in No. 670, although it differed materially therefrom. The other five covered about all of the points which the petitioners argued in the Court of Appeals.

We cannot perceive that the limitation in this Court's grant of certiorari to Question I as "presented by the petition for a writ of certiorari in No. 670" has seriously limited counsel for the petitioners in his statement of the case or argument. They appear to be about the same as they would have been if this Court had granted these petitioners an unlimited writ so that their counsel would have been free to argue all of the six questions specified in his petition for a writ.

STATUTES INVOLVED.

The statutes involved are Section 77 of the Bankruptcy Act (11 U. S. C. § 205) and Section 5 of the Interstate Commerce Act (49 U. S. C. § 5).

The pertinent portions are set forth in full in Appendix A hereto.

STATEMENT OF THE CASE.

For reasons which we will now summarize, we ask this Court to disregard the petitioners' Statement in its entirety. It is not feasible in a brief of reasonable length to correct all of its inaccuracies and omissions.

The respondent's brief in No. 24 contains a statement of the case and we trust that the Court will agree that, since the Court is reviewing only Question No. I as presented in No. 24 and that question is a question of law, no separate statement of the case herein is necessary.

Most of the assertions in the petitioners' Statement are utterly irrelevant to the question presented.

The petitioners' Statement purports to review the whole case factually and historically, as well as with reference to the principal legal questions which were argued by the petitioners in the Court of Appeals. The inappropriateness of the Statement will be obvious from a mere reading of the question presented at pages 4-5 and the Statement at pages 6-21.

For example, the Statement closes (p. 20-21) with assertions which are as plainly irrelevant to the question presented as they are incorrect. It is said (p. 20-21):

> "A truly remarkable aspect of the case is that every presiding officer who heard evidence disapproved the proposed forced merger, and all decisions approving it were by Commissioners or Judges who had neither seen or heard any witnesses and were not as well qualified to evaluate the evidence."

This would be manifestly immaterial, if correct. But it is plainly incorrect.

It is followed by two paragraphs (p. 21) which purport to set forth who heard, and who did not hear, evidence; and those two paragraphs are also incorrect. The best part of a page is thus devoted to immaterial and incorrect assertions on this one point.

"*The* proposed forced merger", to which the petitioners refer, is a Plan which the Commission approved in 1951. The hearings which preceded the approval of the Plan by the Commission were heard before R. T. Boyden, Assistant Director of the Bureau of Finance, and Ralph H. Jewell, Chief, Section of Loans and Reorganization, of the Interstate Commerce Commission.* Assistant Director Boyden did not disapprove the Commission's Plan: the procedure which was followed did not call for the Assistant Director to record his approval or disapproval. The same thing is true of Mr. Jewell; he had made a recommendation in 1946 adverse to a merger *on different terms* but it does not follow that in 1951 he was opposed to the Plan which the Commission then approved.

It is true that the members of the Interstate Commerce Commission and the Judges of the Court of Appeals did not hear witnesses and that Judge Straum did. However, the Court of Appeals found that Judge Straum's findings were "without support in law or in fact" (II, 730; 201 F. 2d 330). And this Court has declined to review the decision of the Court of Appeals that Judge Straum's findings were "without support in law or in fact".**

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* See the transcript of the record of the hearings on July 11-14, 1950 and August 8-17, 1950 which are items 23 and 24 in the Designation of Contents of the Record on Appeal of the respondent (I, 137) and hence included in the unprinted portions of the record in this Court.

** In No. 670 (now No. 24) this Court expressly declined to pass on a question which was put as follows (Petition for certiorari, p. 3):

"II. The second question is whether the findings of Judge Straum that the plan was unfair and inequitable were

If we eliminate the factually incorrect parts of the petitioners' closing paragraphs, all that is left is an assertion that it is "truly remarkable" that the Commission and the Court of Appeals should prevail over Judge STRAUM, inasmuch as Judge STRAUM "heard evidence" whereas the Commissioners and Judges of the Court of Appeals did not.

The petitioners' Statement treats Judge Straum's opinion and findings generally as if they should prevail in this Court not only over the reports and findings of the Commission but over the opinion and findings of the Court of Appeals.

Since in disposing of the petition for certiorari in No. 670 this Court declined to consider whether the Court of Appeals erred in determining that Judge STRAUM's findings were "themselves without support in law or in fact" (II, 729-730; 201 F. 2d 330), the petitioners may not stand on Judge STRAUM's findings or attack those of the Court of Appeals. However, throughout their Statement they do both.

There are no "dogmatic assertions" in the opinion of the Court of Appeals.

Referring to the opinion of the Court of Appeals the petitioners say (p. 7):

> "The other material parts of the opinion are largely a series of dogmatic assertions that the findings of the commission majority are supported by evidence and Judge STRAUM's are not, and that the commission

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so 'clearly erroneous' within the meaning of Rule 52(a) of the Federal Rules of Civil Procedure as to justify the Court of Appeals in setting them aside, and therefore whether the 'cram-down' provision of the 1935 Act, intended only to overcome the dissents of obstructive minorities, should be applied by the courts against the protests of 99% of the security holders who are the equitable owners of the debtor's property."

majority was right and Judge STRAUM was wrong. (201 F. 2d 325)"

The so-called "dogmatic assertions" are statements of conclusions which the Court of Appeals reached after the Court "carefully examined the record made in this and a former hearing" (II, 727; 201 F. 2d 329).

The first is that there is "abundant evidence" to support the Commission's findings on the public interest (*Id.*).

The second group of findings relates to the fairness of the Plan and the reasons for the opposition to it (II, 728; 201 F. 2d 329-330):

> "[The record] shows a most careful and painstaking effort on the part of the commission to properly, adequately, and independently value both the securities held by the bondholders and those to be received by them in exchange and that its finding that the plan was fair and equitable finds full support in the evidence.
>
> "Indeed, an examination of all the testimony now available touching on and dealing with the valuations which under the statute it was for the commission to make, demonstrates, we think, beyond any peradventure that the commission's findings and estimates of the respective future earnings of East Coast and Coast Line and of the present and future values of the securities to be given in exchange for each other was most favorable to the bondholders of East Coast.
>
> "The same careful examination shows that but for the fact, which apparently dominates and controls most of the bondholders in this controversy, that they are primarily concerned not with obtaining value received for their securities but with a conversion of their bonds into a title to the East Coast properties, so that they will own and manage the railroad, all of them would be bound to agree that what they will receive for their bonds under the plan will be of a value equal to, or more than, that of their bonds."

The third relates to Judge STRUM's findings (II, 729-730; 201 F. 2d 330):

> "* * * that the findings of the trial judge, rejecting the commission's findings as to the public interest and as to valuation, and declaring that the plan is unfair and inequitable, are themselves without support in law or in fact."

The minority did not express any disagreement with any of these conclusions of the majority (II, 731-733; 201 F. 2d 331-332).

Presumably the petitioners' counsel characterizes these statements as "dogmatic assertions" because Chief Judge HUTCHESON did not go into greater detail. It is fitting to point out what it would have meant to discuss in detail all of the issues which were before that Court.

The six volumes of the printed record in this Court contain only a relatively small part of the record which was before the Court of Appeals. The transcript of the hearings and arguments before the Interstate Commerce Commission, on which the Commission based its findings, comprises 7,750 pages and there are 489 exhibits; all were included in the unprinted record before the Court of Appeals and are now before this Court.

Judge STRUM wrote a long opinion, in which he said a great many things about the Plan and the Commission (I, 127-168; 103 F. Supp. 825-847). In the Court of Appeals it was not enough merely to show that Judge STRUM's findings were "themselves without support in law or in fact". It was also necessary to show that the Commission's findings were supported by the record and met the statutory requirements. The Court of Appeals concluded that the appellant, the Atlantic Coast Line, did both. The minority of the Court did not indicate any disagreement with the majority as to that.

The briefs in the Court of Appeals totalled over 600

pages; divided about evenly between the two sides.* Extra time was allowed for the argument.

Under these circumstances Chief Judge HUTCHESON said (II, 729; 201 F. 2d 330):

> "It will, therefore, serve no useful purpose for us to take up one by one, as the appellants and appellees have done, to dissect and discuss them, the findings made and reasons given by the commission, on the one hand, and those set out in the lengthy opinion of the trial judge, on the other, to determine our agreement or disagreement with each of them in turn."

The "illusory $4,000,000 cash".

The petitioners' brief says that the Plan provides for an "illusory $4,000,000 cash" (p. 8). The only authority for the assertion is a statement in Judge STRAUM's opinion which the petitioners' counsel quote in a footnote.

Judge STRAUM's statement that the $4,000,000 cash was "illusory" was one of twelve separately numbered reasons which he gave for disapproving the Plan (I, 143-164; 103 F. Supp. 835-846). Each one of those twelve reasons was discussed in detail before the Court of Appeals, including the assertion that the provision for $4,000,000 in cash was "illusory". On this point as on all of the others the majority of the Court of Appeals disagreed with Judge STRAUM and the minority of the Court did not indicate any disagreement with the majority.

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* In addition the Court was asked to review the arguments as to the legality of a so-called "forced merger" which were made in the briefs in the prior appeal. The Southern-Seaboard counsel handed up their 1949 brief (see their brief herein, p. 16) and counsel for the Atlantic Coast Line asked the Court to consider the arguments in the Atlantic Coast Line's 1949 briefs which were on file in the Court.

The petitioners' references to the "price" which Atlantic Coast Line will pay are wholly unwarranted.

The petitioners' brief refers (p. 8) to the "price" which the Atlantic Coast Line will pay as one that "debtor's equitable owners had no voice in fixing, which has never been determined to be the fair value of the property". The brief ignores the fact that after hearings (at which the bondholders introduced testimony) the Commission increased the "price" substantially over that proposed by the Atlantic Coast Line. The petitioners' brief says later (p. 16) that the price fixed by the Commission was only "slightly higher than the one Coast Line had offered to pay", but the difference was clearly substantial (282 I. C. C. 182).

The plan was not objected to in the District Court on behalf of the holders of more than 99% in amount of the First and Refunding Mortgage Bonds, as asserted in the petitioners' brief.

Referring to the holders of the First and Refunding Mortgage Bonds, the petitioners' brief says (p. 10) that the objections to the Plan "were interposed in the District Court on behalf of the holders of more than 99% in amount (103 F. Supp. 833; I, 138)". The only authority for this statement is Judge STRUM's opinion.

The facts are correctly stated in the brief of the petitioners in No. 36, the Successor Mortgage Trustees (p. 6, italics supplied):

> "Insofar as the individual holders of the First and Refunding 5% Bonds are concerned, the record shows that at the time of the hearing in the District Court on the latest plan the holders of slightly less than $35,000,000 face value of the bonds, being 75.5% of the issue, were, by written documents filed with the Court, opposed to the reorganization plan (103 F. Supp. 847). *As to the holders of the remain-*

> *ing $10,000,000, there is admittedly nothing to indicate how they then felt except for the few bonds then represented by a committee (since dissolved) which supported the plan."*

Further detail on this subject will be found at pages 6-9 of the respondent's brief in No. 36.

The assertion that Coast Line would acquire the Debtor's property "at a bargain" is unwarranted.

The petitioners say (p. 13):

> "Coast Line's basic purpose in submitting to the Commission offers to purchase debtor's property, and the basic purpose of the commission majorities in making counter-offers of sale, was to enable Coast Line to acquire at a bargain debtor's double track main line from Jacksonville to Miami. (81 F Supp 934; 179 F 2d 542; 103 F Supp 844)"

The first two references which the petitioners cite do not relate to the present Plan. The only authority for what is said about the present Plan is a statement in Judge STRUM's opinion at 103 F. Supp. 844. As appears above, the majority of the Court of Appeals expressly disagreed with Judge STRUM and the minority of that Court did not indicate that they agreed with him.

The petitioners' quotation of a statement made by the Atlantic Coast Line's President on November 3, 1944 is confusing.

At pages 13-14 the petitioners quote an excerpt from the minutes of a meeting of the Board of Directors of the Atlantic Coast Line which was held on November 3, 1944.* The excerpt consists of portions of a statement made by the President of the Coast Line. The petitioners do not give the date of the meeting and their reference to the

* See St. Joe Paper Company's Exhibit X in Volume III of the record, to be found a little before the middle of the Volume.

President's statement does not disclose the fact that it related to the so-called Lynch plan, which the Commission summarized in its Report of January 8, 1945 (261 I. C. C. 187-193).

The assertions that the Judges of the Court of Appeals did not consider the so-called "consistency clause".

Referring to the views of Chief Judge HUTCHESON and Judge HOLMES on the appeal which was decided in 1950, *Atlantic Coast Line Railroad Company* v. *St. Joe Paper Company*, 179 F. 2d 538, the petitioners say (p. 17):

> "So far as can be ascertained from their respective opinions, neither appellate judge gave any consideration to the effect of the 'consistency' clause in § 77(f), * * *."

Then, referring to the opinion which was handed down in 1953, the petitioners say (p. 20):

> "This opinion, too, fails to disclose that any consideration was given to the limitation of power imposed on the Commission by the 'consistency' clause in § 77(f)."

There is no justification for any suggestion that on either of the two appeals the Judges of the Court of Appeals did not consider the "consistency clause". The clause had been specifically mentioned with some prominence by Judge SIBLEY (V, 475-476; 81 Fed. Supp. 932), and was the subject of extensive arguments, both in the briefs and orally, in the Court of Appeals in 1949. In 1952 the Judges were asked to consider the briefs which were filed on both sides in 1949. There is no more ground for saying that the majority of the Court did not consider the "consistency clause" than there would be for saying that the minority did not consider *any* of the provisions in Section 77—for neither of Judge RUSSELL's opinions

mentioned any of the provisions of Section 77 (179 F. 2d 545; II, 731-733; 201 F. 2d 331-332).

The petitioners' description of the case as involving offers and counter-offers by the Atlantic Coast Line and the Interstate Commerce Commission reflects a complete misconception.

The assertion that even "at this late date Coast Line is not bound" is incorrect in fact and in law.

The petitioners' brief contains many references to what their counsel choose to call offers or counter-offers by the Commission and the Atlantic Coast Line as if the case involved a private contract between the Commission and the Coast Line (p. 7, 8, 15, 16, 18, 19). Any such view of the case reflects a fundamental misconception.

A correct analysis will be found in the Commission's Third Supplemental Report, in which the Commission said (267 I. C. C. 305):

> "The Coast Line entered the picture as a connecting trunk line, willing to operate the debtor as part of its system and to issue to the creditors securities of its own of the ascertained value of the claims surrendered by them. It has been admitted as a party to the proceedings by us pursuant to our authority and duty to promulgate a plan which is not only fair and equitable to the creditors but compatible with the public interest in the maintenance of an adequate transportation system. This is in full accord with the theory of the act. Under the statute we are charged with the dual duty of promulgating a plan which will be fair and equitable to the creditors and which will be compatible with the public interest. In our informed judgment, we must determine the value of the property, and this value, expressed in terms of securities or cash, is distributed to the creditors in the order of their priority. Claims in excess of such value, including the interest of the stockholders, are treated as worthless."

The petitioners say (p. 8):

> "Even at this late date Coast Line is not bound. It is free to withdraw at any time. There is not and cannot be an enforceable contract between Coast Line and the commission majority."

The Atlantic Coast Line's Exhibit 10, which will be found in Volume III of the record about one-quarter of the way through, shows that on November 15, 1951 the Board of Directors of the Atlantic Coast Line Railroad Company adopted the Plan and authorized the officers of the Company to take appropriate steps to secure the assent of the stockholders; on December 20, 1951 the Board called a special meeting of stockholders; and on January 15, 1952 a special meeting voted to accept the Plan and to assent to its terms. The record of these various steps was referred to at the hearing before Judge STRUM by counsel for the Atlantic Coast Line as having made the Plan "binding" (II, 273-274) and no question has previously been raised as to the binding force of the steps thus taken by the Coast Line's Board of Directors and stockholders.

The petitioners' Statement is silent about the reasons which the petitioners, of whom E. N. Claughton is the leader, have for collaborating with and supporting the St. Joe Paper Company and the duPont Trustees.

The petitioners are usually referred to as the Welbon Group or the Claughton Group. The leader of the Group is Edward N. Claughton, who testified before Judge SIBLEY in 1949 (IV, 297-319) and at the Commission hearing in July, 1950 (Tr. 5327-5353).* Counsel for the Group always puts the name of W. G. Welbon first, but Claughton has been the leader.

* These references are to the transcript of the Interstate Commerce Commission hearings in July, 1950, which are part of the unprinted portion of the record (I, 197).

Before Judge SIBLEY, the Group consisted of six men (IV, 43, 297-298). At the time of the Commission hearings in July, 1950 there were only four (282 I. C. C. 94; Tr. 5327-5328).* When the time came to file objections to the present Plan is December, 1951, there were only three, E. N. Claughton, A. W. Corbett and W. G. Welbon (I, 24, 45).

The members in the Group, and Claughton in particular, have been heavy speculators in the First and Refunding Mortgage Bonds and it appears that their speculations have been financed by loans made by one or more of the Florida National Group of Banks, which are controlled by the duPont Trustees (267 I. C. C. 315).

On December 10, 1948 Claughton testified that he owned approximately $3,500,000 of Bonds (IV, 299). When he went on the stand before Judge SIBLEY on January 11, 1949, he testified that he then owned $3,100,000 (IV, 298), of which $2,599,000 were pledged with the Florida National Bank at Miami (IV, 300). The Florida National Bank at Miami is controlled by the St. Joe Paper Company (267 I. C. C. 315).

Claughton further testified on January 11, 1949 about the holdings of the other five members of the Group which at that time totaled $1,400,000 (IV, 298-299). On cross-examination he said that all of the other members of the Group had had loans in the past from one or more members of the Florida National Group of Banks; that he did not know whether they all had such loans at that time; but he thought some of them did not (IV, 300-301). The Group's holdings as shown before Judge SIBLEY totaled $4,500,000, of which $3,100,000 were Claughton's and $1,400,000 were the others'.

When Claughton testified at the Commission hearing on July 11, 1950, it appeared that

(1) the Claughton Group, which consisted of six men in January, 1949, had been reduced to four men and their

aggregate holdings had been reduced to $793,000 (Tr. 5247, 5327-5328); and

(2) *Claughton, who had held $3,100,000 of Bonds at the time of the hearing before Judge Sibley in the District Court on the Previous Plan* (IV, 298), *had reduced his holdings to $2,000 principal amount* (Tr. 5248, 5342).

By the time of the hearings before Judge STRUM members of the Claughton Group had apparently made some additional purchases. No testimony was given before Judge STRUM about the various holdings of the Claughton Group and other groups (there were merely statements by counsel), but counsel for the Claughton Group said that they held $1,220,000 of Bonds (II, 257). Later during the hearing before Judge STRUM counsel for the Group said (II, 357):

> "Discussions which were in progress prior to the time that the hearing began resulted in my being employed to represent an additional one million dollars par value of the five percent bonds held by a group of bondholders."

Apparently the holders of the additional $1,000,000 were not Claughton, Corbett or Welbon but some other bondholder or bondholders. The record does not show who they were.

The record establishes that Claughton and Edward Ball, duPont Trustee and former President of the St. Joe Paper Company, have been associated in business enterprises in the past, although Ball's testimony on this subject justified the Commission's reference to him as "vague, indefinite and adroit" (Tr. 3587-3589*; 267 I. C. C. 316-317).

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* This reference is to the transcript of the Interstate Commerce Commission hearing on November 27, 1945, which is included in the unprinted portion of the record (I, 183).

SUMMARY OF THE ARGUMENT

1. The petitioners have no interest distinct from that of the St. Joe Paper Company in establishing the proposition that the holder of a majority in amount of the First and Refunding Mortgage Bonds can block any merger plan.

Their argument is simply another argument for the St. Joe Paper Company.

The record indicates the reasons why they support the St. Joe Paper Company and oppose the Commission's Plan.

2. The petitioners' argument that the Commission did not have power to approve the so-called "forced merger plan" is untenable.

3. The petitioners' contention that "the 5% bondholders are debtor's equitable owners and in that capacity are entitled to vote under § 5(11) of the Interstate Commerce Act on the question of corporate asset by debtor to the merger, consolidated or transfer" is also untenable.

4. The petitioners' contention that the cram-down provision of Section 77(e) of the Bankruptcy Act conferred no power on the Commission is irrelevant.

5. The petitioners' arguments based on the *Boyd* case are manifestly insubstantial and plainly too remote from the question at issue to merit consideration.

ARGUMENT.

PRELIMINARY POINT.

The petitioners have no interest distinct from that of the St. Joe Paper Company in establishing the proposition that the holder of a majority in amount of the First and Refunding Mortgage Bonds can block any merger plan.

Their argument is simply another argument for the St. Joe Paper Company.

The record indicates the reasons why they support the St. Joe Paper Company and oppose the Commission's Plan.

The proposition asserted by the petitioners is that Section 77 "precludes the approval or certification by the Commission of a plan of reorganization providing for a merger, consolidation or transfer which has not been consented to by the requisite majority of the debtor's equitable owners" (p. 26). Throughout the petitioners treat the holders of the First and Refunding Mortgage Bonds as the "debtor's equitable owners" but at this juncture we need not consider the meaning of the words "equitable owners". The important thing is that petitioners speak specifically of *"the requisite majority"*.

The St. Joe Paper Company holds, and has held for years, a majority in amount of the First and Refunding Mortgage Bonds. Hence the petitioners' proposition, simply stated, is that so long as the St. Joe Paper Company continues to hold a majority of the First and Refunding Mortgage Bonds the Commission cannot approve a plan of reorganization providing for a merger, consolidation or transfer without the consent of the St. Joe Paper Company.

It is easy to see why the St. Joe Paper Company has an interest in sustaining that proposition. A rule under which the holder of a majority in amount of a class of bonds such as the First and Refunding Mortgage Bonds could block a plan of reorganization providing for a merger,

consolidation or transfer would lodge a very important power in the majority holder. In this case such a rule would be greatly to the liking of the St. Joe Paper Company which, as Chief Judge Hutcheson twice said (179 F. 2d 544; II, 727; 201 F. 2d 329), bought a majority in amount of the Bonds in order to control the Florida East Coast Railway Company.

However, the establishment of such a rule would not lodge any power in a minority bondholder, or in a group of bondholders which did not, taken together, hold a majority of the bonds. What interest have minority bondholders generally in sustaining such a proposition? What interest have the Welbon (Claughton) Group in sustaining the proposition in this case?

The theory that a minority bondholder is better off if the holder or holders of a majority can block a "merger plan" presupposes that minority bondholders can generally rely for their protection on a majority bondholder or bondholders and cannot generally rely on the Interstate Commerce Commission and the Courts under Section 77 of the Bankruptcy Act. Yet normally a unification by a merger, consolidation or transfer of assets can be expected to be advantageous to all those who are affected by it and Section 77 reorganizations providing for mergers ought to be advantageous to minority bondholders if the terms are fair. And there can be very serious conflicts of interests between a majority bondholder and minority bondholders. This was eloquently pointed out on several occasions by counsel for the petitioners in No. 33,* and needs no elaboration here.

In this case the record and findings of the Court of Appeals create the strongest presumption, which the petitioners do not really attempt to rebut, that the interests of the minority bondholders will be served by the Commis-

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* See respondent's brief in No. 33, p. 12-15.

sion's Plan.* Furthermore, it is definitely established that the majority bondholder, St. Joe Paper Company, has a distinct and particular interest in blocking a merger plan: it wishes to control an independently reorganized Florida East Coast Railway Company.

The petitioners' brief is completely silent about any conflict of interests between the majority bondholder and the minority bondholders arising out of the majority bondholder's insistence on control or anything else. Throughout the brief the petitioners speak of "the equitable owners" and "the bondholders" as if they constituted a single interest.

In effect their argument is simply another argument for the St. Joe Paper Company.

We think the record which we have reviewed above at pages 16-18 shows clearly why they support the St. Joe Paper Company so unreservedly. In 1949 Claughton took the stand before Judge Sibley and undertook to justify his opposition to the Previous Plan (IV, 297-319). In 1952 before Judge Strum, when the objections to the present Plan were heard, neither Claughton nor any other petitioner took the stand. We are certainly entitled to infer from the record referred to above at pages 16-18 that they have collaborated so closely with the St. Joe Paper Company because of their close business relations with the duPont Trustees, the St. Joe Paper Company and the Florida National Group of Banks.

Even if our inference should be incorrect, it would still be true that the argument which the petitioners advance is a majority bondholder's argument, not a minority bondholder's argument.

* * * * *

The foregoing observations naturally raise the question why it is necessary or proper for the petitioners to have filed any brief at all.

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* See the respondent's brief in No. 36, p. 6-13.

The real party in interest, the St. Joe Paper Company, is represented in No. 24 by counsel of preeminent distinction. His associate counsel include attorneys for the St. Joe Paper Company who are able and experienced and have been in this case for more than ten years. In addition, distinguished counsel for the Southern and Seaboard have fully argued the proposition that a so-called "forced merger" is unauthorized and they are the same counsel who took the lead in arguing that proposition before Judge SIBLEY and in the Court of Appeals. We do not recollect that counsel for the Welbon (Claughton) Group has ever argued the question before either in a brief or orally.

The extent to which we will reply to the petitioners' brief will be to some extent affected, we submit properly, by the considerations which we have just summarized.

I.

The petitioners' argument (p. 36-43) that the Commission did not have power to approve the so-called "forced merger plan" is untenable.

In large part the petitioners' arguments follow those of the petitioners in No. 24. For that reason we will refer generally to the respondent's brief in No. 24 and will deal for the most part herein with arguments made by the petitioners herein that are not mere duplicates of those in No. 24.

We agree with the petitioners that Thompson v. Texas Mexican Railway Co. (1946) 328 U. S. 134 is a good example of the integration of Section 77 and the Interstate Commerce Act.

The petitioners' brief says that the integration of Section 77 and the Interstate Commerce Act "is demonstrated in *Thompson* v. *Texas Mexican R Co*, 328 U. S. 134 (1946)" (p. 27). They quote *in part* the statement in Justice

DOUGLAS' opinion that carriers which are being reorganized under Section 77 are not exempt from the provisions of Section 1(18) of the Interstate Commerce Act.* The opinion says this (p. 144):

> "Carriers being reorganized under § 77 of the Bankruptcy Act are not exempt from that provision. § 77(o) 11 U. S. C. § 205(o); *Warren* v. *Palmer*, 310 U. S. 132, 137-138."

Section 77(o) authorizes abandonments during the pendency of the proceeding (independently of a plan) "only with the approval and authorization of the Commission when required by the Interstate Commerce Act as amended February 28, 1920, or as it may be hereafter amended". The implication in the petitioners' brief seems to be that the integration of Section 77 and Section 1(18) of the Interstate Commerce Act is effected by the "consistency clause" of subsection (f) of Section 77. Actually the integration results from the specific provision of subsection (o) and petitioners' brief simply omit this Court's reference thereto.

Thompson v. *Texas Mexican Railway Co.* also held (p. 145):

> "There is no requirement in Section 1(18) that the application be made by the carrier whose operations are sought to be abandoned. It has been recognized that persons other than carriers 'who have a proper interest in the subject matter' may take the initiative. See *Atchison, T. & S. F. R. Co.* v. *Railroad Commission*, 283 U. S. 380, 393-394."

This Court's two holdings, taken together, illustrate the integration of Section 77 and the Interstate Commerce Act with respect to *the protection of the public interest*. They also establish that, at least under Section 1(18), it is not necessary to have an application initiated by "the carrier whose operations are sought to be abandoned".

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* Section 1(18) is quoted in full at page 2 of the Southern-Seaboard brief in number 24.

As appears in the Southern Seaboard brief (p. 2), Section 1(18) prescribes that "there shall first have been obtained" a certificate thereunder—it does not say that the carrier whose operations are to be abandoned must itself apply for the certificate. Similarly, as we point out in the respondent's brief in number 24 (p. 71-72), Section 5(2) does *not* prescribe that a carrier whose properties are to be acquired must itself file an application under Section 5(2).

The Commission properly stated the relationship between Section 77 and Section 5(2) of the Interstate Commerce Act in its Third Supplemental Report of April 8, 1947, when it said (267 I. C. C. 308):

> "The Coast Line plan, by which control would be transferred to that carrier, is in effect a request or application to us by one carrier for authority to acquire control of another and, in conformity with the provisions of subsection (f) of Section 77 of the Bankruptcy Act that the transfer of the properties of a debtor be not inconsistent with the provisions and purposes of the Interstate Commerce Act, the record should contain the information required in a proceeding under section 5(2) of the Interstate Commerce Act."

The petitioners say that one of the Commission's holdings in the Fourth Supplemental Report is to be contrasted with what the Commission said in the Third Supplemental Report (p. 28), but there is clearly no conflict between the two.

The petitioners' references to offers and counter-offers by the Commission and the Atlantic Coast Line and the discussion of "arms-length bargaining" reflect fundamental misconceptions of Section 77.

At pages 26-43 of the petitioners' brief there are repeated references to offers and counter-offers as if this case involved a private contract between the Interstate

Commerce Commission and the Atlantic Coast Line (see p. 28, 34, 35). In our statement of the case (p. 15-16) we have pointed out that this approach by the petitioners reflects a fundamental misconception of the case.

An equally fundamental misconception is reflected by counsel's emphasis on "arms-length bargaining" (p. 28, 32, 33), "an owners' bargaining approach" (p. 33) and "an owner's bargaining latitude" (p. 33). We are not even dealing here with a single owner of the Debtor's property. We are considering the respective powers under Section 77 of a holder of a majority in amount of the First and Refunding Mortgage Bonds, on the one hand, and the Interstate Commerce Commission and the Courts on the other hand. The essence of the petitioners' argument is that in this case there should have been "arms-length bargaining" between the St. Joe Paper Company and the Atlantic Coast Line; that if such "arms-length bargaining" had resulted in an agreement on a plan, then it would have been proper for the Commission and the Courts to approve the plan; and that, absent such an agreement between the St. Joe Paper Company and the Atlantic Coast Line in advance of the Commission's action on the plan, the Commission had no power to approve the Plan which it did approve. There is no support for this in Section 77 and the argument conflicts directly with the philosophy and most important objectives of Section 77 which we have summarized at pages 96-104 of the respondent's brief in No. 24.

The petitioners' arguments about the bankruptcy power and the commerce power under the Constitution are wholly untenable.

Any analysis of the bankruptcy power and the commerce power confirms the conclusion, which must be reached after reading Section 77, that the Commission had the power to approve the Plan in this case.

The petitioners' brief says (p. 38, footnote omitted):

> "The basic reason for the limitation is that the power of congress to provide for the relief and rehabilitation of financially distressed railroads flows from the bankruptcy power, while the commerce power is the source of the power to regulate mergers, consolidations and transfers, and the latter had been the subject matter of much controversy and legislation prior to the enactment of Section 77 in 1933."

The footnotes, which we have omitted, quote the provisions of Article 1, § 8, clauses 4 and 3, of the Constitution.

The petitioners' first premise is that "the power of the Congress to provide for the relief and rehabilitation of financially distressed railroads flows from the bankruptcy power" (p. 38). While we are at a loss to know why the interstate commerce power may not cover, at least to some extent, the rehabilitation of financially distressed railroads, and we believe the power to enact Section 77 flows from both the bankruptcy clause and the interstate commerce clause*, we have no doubt that Section 77 may properly be regarded as resting primarily on the bankruptcy clause.

Counsel say (p. 38) that "the commerce power is the source of the power to regulate mergers, consolidations and transfers". In the case of a bankrupt railroad, like the Florida East Coast, a merger, consolidation or transfer of the debtor's assets is a means of realizing on the bankrupt's property for the benefit of the bankrupt's creditors, as well as providing for such transportation operations as may be compatible with the public interest. Certainly the bankruptcy clause of the Constitution is broad enough to cover legislation which controls the methods of realizing on the assets of a bankrupt. Article X of Chapter X contains

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* Because of the definition of "railroad corporation" in subsection (m) of Section 77 that Section applies only to a "common carrier railroad engaged in the transportation of persons and property in interstate commerce".

in Section 216(10) provisions which are very similar to those in Section 77(b)(5) and Chapter X rests solely on the bankruptcy power.*

We suggest that the following is a correct analysis of the relationship of the two constitutional powers and the two acts, Section 77 and the Interstate Commerce Act:

> The power to regulate mergers, consolidations and transfers of *solvent* carriers flows from the interstate commerce power, and the Interstate Commerce Act, which is an exercise of that power, deals with that subject.
>
> Insofar as the participation of a bankrupt railroad, its stockholders or creditors, in a merger, consolidation or transfer of assets impinges upon the private rights of the bankrupt corporation, its stockholders or creditors, the bankruptcy power is dominant, although the interstate commerce power can support legislation with respect thereto. Section 77 deals with the private rights of bankrupts, their stockholders and creditors—it was enacted for that purpose. The Interstate Commerce Act does not deal with the private rights of bankrupt carriers, their creditors or stockholders.
>
> Section 77 and the Interstate Commerce Act both authorize transactions which affect the public interest. At least many of the same factors are present in any merger, consolidation or transfer of assets whether it involves only solvent carriers or whether one or more insolvent carriers be involved. Section 77 contemplates that, as respects the public interest, there shall be consistency between action taken under Section 77 and action taken under the Interstate Commerce Act.

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* See 11 U. S. C., Section 616.

II.

The petitioners' contention (p. 43-50) that "the 5% bondholders are debtor's equitable owners and in that capacity are entitled to vote under § 5(11) of the Interstate Commerce Act on the question of corporate assent by debtor to the merger, consolidation or transfer" is untenable.

The proposition that the bondholders are the "equitable owners" of "*the* property" raises three questions:

What is meant by the words "*the* property"? Certainly the bondholders are not the equitable owners of the unmortgaged assets, which the Commission valued at well over $1,000,000 (282 I. C. C. 176-181). Properties worth over $1,000,000 are not so insignificant that their existence can be ignored and the fact that the First and Refunding Mortgage does not cover all of the Debtor's property points up one of the many respects in which the terminology used by the petitioners is incorrect or ambiguous.

The other two questions can best be considered together. What is the meaning of the words "equitable owners"? What rights do equitable owners have?

The bondholders are not stockholders of a solvent railroad corporation.

The petitioners, in characterizing the bondholders as "equitable owners", rely on *Helvering* v. *Alabama Asphaltic Limestone Co.* (1942) 315 U. S. 179, *Helvering* v. *Cement Investors, Inc.* (1942) 316 U. S. 527 and *Helvering* v. *New Haven & S. L. R. Co.* (C. C. A. 2, 1941) 121 F. 2d 985, cert. den. (1942) 315 U. S. 803 reh. den. (1942) 315 U. S. 829.* Those cases held that for the purposes of the "continuity of interest" rule, which qualifies the definition of "reorganization" for Federal income tax purposes, *creditors who became stockholders of a new corporation* should be per-

* In footnote 32 at page 44 counsel for petitioners also cite *Bondholders Committee* v. *Commissioner* (1942) 315 U. S. 189.

mitted to "date their equity ownership from the time when they invoke the processes of the law to enforce their rights of full priority" (315 U. S. at p. 184).

However, in *Helvering* v. *Southwest Consolidated Corp.* (1942) 315 U. S. 194, decided the same day as *Alabama Asphaltic Limestone Co.*, this Court held that, for the purposes of clause C of § 112 (g) (1) of the Revenue Act of 1934, creditors could not be deemed "stockholders", distinguishing *Alabama Asphaltic Limestone Co.* as follows (315 U. S. at p. 202):

> "But it is one thing to say that the bondholders 'stepped into the shoes of the old stockholders' so as to acquire the proprietary interest in the insolvent company. It is quite another to say that they were the 'stockholders' of the old company within the purview of clause C."

At the very least this latter opinion brings out that, even if in a given situation it would be permissible to characterize bondholders as "equitable owners" of a debtor's property, it does not follow that as equitable owners they possess all the rights and immunities of stockholders of a solvent corporation. Indeed, *Southwest Consolidated Corp.* indicates that bondholders cannot be deemed stockholders for the purposes of a statute which refers to stockholders *eo nomine* unless they are in fact stockholders *at the time;* it is not enough that they may have the right to become stockholders in the same or another corporation or, indeed, that they may later do so.

Proceeding from the premise (p. 47) that the holders of the First and Refunding Mortgage Bonds "stepped into the shoes" of the Debtor's stockholders either in 1932, when their trustees brought the foreclosure suit and secured the receivership, or in 1941, when they instituted the Section 77 proceeding", counsel for the petitioners argue (p. 48):

> "In those shoes, and in the exercise of the rights acquired by stepping into them, they are entitled to vote under § 5(11) of the Interstate Commerce Act

> on the question of corporate assent by debtor to the proposed merger, consolidation or transfer. The proposed merger, consolidation or transfer cannot be forced or effectuated without 'the assent • • • of a majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the' 5% bonds (§5(11))."

This contention points up an important issue sharply:

> Despite the fact that a primary purpose of Section 77 of the Bankruptcy Act is to modify the rights of stockholders and creditors of a debtor railroad corporation and although Section 77 provides expressly that any plan of reorganization which calls for a merger, consolidation or transfer of assets may be confirmed over the objection of creditors, does a purchaser (or other holder) of a majority in amount of an issue of mortgage bonds of an insolvent debtor become the legal equivalent of a majority stockholder of a solvent railroad corporation and for that reason entitled to rights which may be accorded by the Interstate Commerce Act to stockholders of solvent railroad corporations?

Even if *Southwest Consolidated Corp.* had never been decided, *Alabama Asphaltic Limestone Company* and the related cases would not establish that the holders of the First and Refunding Mortgage Bonds are *now* entitled to be treated as stockholders of a solvent railroad corporation. *Alabama Asphaltic Limestone Company* and the other cases involved bondholders who actually became stockholders under plans of reorganization which had been consummated. The question was whether the ownership of the equity which they actually obtained should be deemed to relate back, *for tax purposes*, to an earlier date. The holders of the First and Refunding Mortgage Bonds have not become stockholders. In particular, the St. Joe Paper Company, which is the holder of the majority

in amount of the First and Refunding Mortgage Bonds, has not become a majority stockholder.

Alabama Asphaltic Limestone Company and the other cases relied upon by the petitioners did not involve interstate railroads and the outcome of the reorganization proceedings in those cases was more or less automatic. The outcome of a reorganization proceeding under Section 77 involving an interstate railroad is not automatic in any sense and cannot be assumed in advance. Justice REED said for this Court in *Ecker* v. *Western Pacific Railroad Corp.* (1943) 318 U. S. 448, 468:

> "These reorganizations require something more than contests between adversary interests to produce plans which are fair and in the public interest. When the public interest, as distinguished from private, bulks large in the problem, the solution is largely a function of the legislative and administrative agencies of government with their facilities and experience in investigating all aspects of the problem and appraising the general interest. Congress outlines the course reorganization is to follow. It established standards for administration and placed in the hands of the Commission the primary responsibility for the development of a suitable plan. When examined to learn the purpose of the enactment Section 77 manifests the intention of Congress to place reorganization under the leadership of the Commission, subject to a degree of participation by the Court."

With respect to control, the same opinion said, referring to the 1935 revision of Section 77 (p. 471):

> "The Senate Report, No. 1336, 74th Cong., 1st Sess., concluded:
>
> "The amendments to section 77 leave unimpaired the power and the duty of the commission and the courts to deal with the most important feature of all reorganization plans, that of the control of the reorganized company; and similarly the commission

and courts will continue to have the power and authority of making that thorough investigation which is necessary to assure sound and reliable control for bankrupt companies when they emerge from the courts, in place of the type of control under which some railroads have been wrecked."

True it is that, if there were an internal plan of reorganization with a ratable distribution of the stock among the holders of the First and Refunding Mortgage Bonds, the St. Joe Paper Company would own a majority of the stock and would control the reorganized company. But that has not happened. And to say *now* that this Court should view the situation *as if it had happened* is to suggest that powers of the Commission and the Courts expressly granted by Section 77 should be emasculated, that it must be assumed that the St. Joe Paper Company *has a right to be* a majority stockholder of a reorganized Florida East Coast and that the St. Joe Paper Company is entitled *now* to all the rights and immunities of a majority stockholder of a solvent corporation.

The proposition that the bondholders of a bankrupt railroad corporation should be treated as the stockholders of a solvent corporation for the purposes of a statute which refers expressly to the stockholders of the railroad corporation would seem extraordinary enough, as well as in conflict with this Court's decision in *Southwest Consolidated Corp.* However, the petitioners must go further. This is a proceeding under Section 77 of the Bankruptcy Act, the provisions of which deal explicitly with the rights of bondholders in such a proceeding, and to sustain the petitioners' argument it is necessary not merely first to read something into the Interstate Commerce Act which is not there but also to take the affected parts of the Interstate Commerce Act and then read them into Section 77 in the altered form.

The reference in Section 5(11) of the Interstate Commerce Act to a vote of stockholders is immaterial to any issue in this case.

As already noted, the petitioners stress the provisions of Section 5(11) of the Interstate Commerce Act (p. 48-50; see also p. 53). The text of Section 5(11) will be found in Appendix A (p. ix). It was considered by this Court in *Schwabacher* v. *United States* (1948) 334 U. S. 182.

None of the petitioners in No. 24 relies on Section 5(11) at all.

Section 5(11) contains a provision in parentheses with respect to "the votes of holders of the shares entitled to vote of the capital stock of [a corporation participating in the transaction] at a regular meeting of such stockholders, the notice of such meeting to include such purpose, or at a special meeting called for that purpose". This provision was added to the Interstate Commerce Act by the Transportation Act of 1940 (54 Stat. 899, 908).

To hold that Section 5(11) affects the issue herein materially it would be necessary to find that when the Congress added Section 5(11) to the Interstate Commerce Act in 1940 and spoke of "the votes of the holders of the shares entitled to vote of the capital stock" of a corporation it meant, in the case of an insolvent corporation, such *bondholders* as might be considered to be the equitable owners of the corporation's properties and that the rights of the bondholders of bankrupt corporations, as established by Section 77 of the Bankruptcy Act, were enlarged accordingly.

It also would be necessary to hold that one of the purposes of Section 5(11) was to *prevent* a merger, consolidation or transfer of assets in the absence of the vote referred to in the parenthetical phrase.

Can it be seriously suggested that if Section 77, prior to the addition of Section 5(11) to the Interstate Commerce Act, authorized the Commission to approve a plan of

reorganization providing for a merger, consolidation or transfer of the assets of the Debtor over the objection of the holder of a majority of the amount of the First and Refunding Bonds, the addition of Section 5(11) to the Interstate Commerce Act in 1940 took that power away from the Commission?

The petitioners say that "no one would be so bold as to urge that the assent of the stockholders would not be required under Section 5(11) of the Interstate Commerce Act" for a merger plan under Section 77 if the debtor were merely "unable to meets its debts as they mature" and not insolvent in the bankruptcy sense (p. 48). While there is no need to argue about the rights of stockholders in such a contingency, we have no doubt that, if a debtor has recourse to Section 77, the provisions of Section 77 apply and that no assent of stockholders is required because of the provisions of Section 5(11) of the Interstate Commerce Act.

The petitioners' contentions about two votes of "equitable owners" constitute a reductio ad absurdum of the petitioners' main argument.

The petitioners argue at page 49, and again at pages 53-54, that if the equity of the stockholders of a debtor is going to be held to be without value and a plan is to provide for a merger, consolidation or transfer of assets, then there have to be two votes by the "equitable owners" —one "at a regular or special meeting, on the question of corporate assent" and the other on the submission under Section 77 (p. 53-54). This interpretation of Section 77 is discussed in the respondent's brief in No. 24 at pages 91-94. It is fantastic.

III.

The petitioners' contention (p. 50-51) that the cram-down provision of Section 77(e) of the Bankruptcy Act conferred no power on the Commission is irrelevant.

At pages 50-51 counsel for the petitioners purport to summarize the Commission's "thought process". The whole discussion reads as if there were an explicit provision in Section 77 that the Commission could approve "only carrier-initiated, voluntary mergers, consolidations or transfers which are consented to by the equitable owners of each railroad involved". There is not.

The argument that the cram-down provision "conferred no power on the Commission" is irrelevant. "The judicial process in bankruptcy proceedings under § 77 is, as it were, brigaded with the administrative process of the Commission." *Palmer* v. *Massachusetts* (1939) 308 U. S. 79, 87. No one familiar with *Reconstruction Finance Corporation* v. *Denver & Rio Grande Western Railroad Co.* (1946) 328 U. S. 495 and what has happened since Congress enacted the cram-down provision can doubt that the cram-down provision has greatly increased the *combined* powers of the Commission and the Court. This point is covered more fully at page 62 of the respondent's brief in number 24.

IV.

The petitioners' argument (p. 52-63) that "the Court's 'cram-down' power does not authorize confirmation of the so-called 'forced merger' plan of reorganization" is also untenable.

The petitioners' brief says (p. 52) that Chief Judge Hutcheson made a "gratuitous and completely erroneous construction of the cram-down provision in § 77(e)".

The charge that Chief Judge Hutcheson's construction of the cram-down provision was "gratuitous" is presumably based on the fact that at the time the Plan was not up for confirmation. However, the appellees in the Court of

Appeals (now petitioners in the four cases in this Court) went into the whole subject of the effect of opposition (or the absence of consent) to a plan of reorganization under Section 77. What Judge Hutcheson did was to summarize this Court's holding in *Reconstruction Finance Corporation* v. *Denver & Rio Grande Western Railroad Co.* (1946) 328 U. S. 495, 531-535.

The petitioners' argument at pages 52-56 deals largely with the *two votes* which they say have to be taken by the "equitable owners". We referred to that subject at page 35 above and it is discussed more fully at pages 91-94 of the respondent's brief in No. 24.

The arguments in the balance of this section of the brief are so plainly untenable and so far removed from the question on which this Court has granted certiorari that they require no answer.

V.

The petitioners' arguments (p. 63-71) based on the *Boyd* case are manifestly insubstantial and plainly too remote from the question at issue to merit consideration.

One of the questions on which the petitioners sought certiorari in No. 710 was stated in their petition as follows (p. 12, footnote omitted):

> "5. If § 77 authorizes the 'forced merger' plan and is constitutional, does the plan violate the absolute priority rule of the Boyd and later cases by appropriating the 5% bondholders' security to the payment of Coast Line's unsecured claim?"

In their brief in support of the petition they argued that (p. 24-25):

> "The decision of the Court of Appeals that the fourth plan does not violate the absolute priority rule conflicts with principles enunciated by this Court in the Boyd and later cases."

The respondent answered their argument in its brief in opposition to the writ (p. 16-17), which referred to the respondent's brief in No. 702 (p. 11-15), since the petitioners in No. 702 had also asked for a writ of certiorari to review the question whether there was a violation of the rule of the *Boyd* case.

These petitioners now make quite a long argument about the *Boyd* case. The argument is manifestly insubstantial, and it is so plainly outside of the scope of the question which this Court has agreed to review that there would be no justification for burdening the Court with an answer to it.

CONCLUSION.

The order of the Court of Appeals should be affirmed.

Dated, October 5, 1953.

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Appendix A

i

THE STATUTES

Attributes of a Plan of Reorganization.

SECTION 77(b)—first paragraph in full.[1]

(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; (5) shall provide adequate means for the execution of the plan, which may include *the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations*, the retention of all or any part of the property by the debtor, the sale of all or any part of the property of the debtor either subject to or free from any lien at not

[1] The text of all Section 77 provisions is taken from 11 U. S. C. A. § 205. Italics are supplied.

less than a fair upset price, the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein, the satisfaction or modification of any liens, indentures, or other similar interests, the curing or waiver of defaults, the extension of maturity dates of outstanding securities, the reduction in principal and/or rate of interest and alteration of other terms of such securities, the amendment of the charter of the debtor, and/or the issuance of securities of either the debtor or any such other corporation or corporations for cash, or in exchange for existing securities, or in satisfaction of claims or rights or for other appropriate purposes; and may deal with all or any part of the property of the debtor; may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; *and may include any other appropriate provisions not inconsistent with this section.*

Approval of a Plan by the Commission.

SECTION 77(d)—first paragraph in part.

• • • the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions.

Approval of a Plan by the Court.

SECTION 77(e)—first paragraph and first sentence of second paragraph.

(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties

in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor,

and he shall enter an order in which he may either dismiss the proceedings or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received.

Confirmation of a Plan—the "Cram-down" Provision.

SECTION 77(e)—third paragraph in part.

Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interest or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e):* • • •.

The So-Called "Consistency Clause".

SECTION 77(f)—fifth sentence

Upon confirmation of a plan, the Commission shall, without further proceedings, grant authority for the issue of

any securities, assumption of obligations, transfer of any property, sale, consolidation or merger of the debtor's property, or pooling of traffic, to the extent contemplated by the plan and *not inconsistent with the provisions and purposes of chapter 1 of Title 49 as on August 27, 1935, or thereafter amended.*

Section 5 of the Interstate Commerce Act—Pertinent Provisions.[1]

UNIFICATIONS, MERGERS, AND ACQUISITIONS OF CONTROL

(2) (a) *It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision* (*b*)—

(i) *for two or more carriers to consolidate or merge their properties or franchises, or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership; or for any carrier,* or two or more carriers jointly, *to purchase,* lease, or contract to operate *the properties,* or any part thereof, *of another;* or for any carrier, or two or more carriers jointly, to acquire control of another through ownership of its stock or otherwise; or for a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise; or

(ii) for a carrier by railroad to acquire trackage rights over, or joint ownership in or joint use of, any railroad line or lines owned or operated by any other such carrier, and terminals incidental thereto.

(b) *Whenever a transaction is proposed under subparagraph* (*a*), *the carrier* or carriers or person *seeking*

[1] The text is taken from 49 U. S. C. A. § 5. Italics are supplied.

authority therefor shall present an application to the Commission, and thereupon the Commission shall notify the Governor of each State in which any part of the properties of the carriers involved in the proposed transaction is situated, and also such carriers and the applicant or applicants (and, in case carriers by motor vehicle are involved, the persons specified in section 305 (e)), *and shall afford reasonable opportunity for interested parties to be heard.* If the Commission shall consider it necessary in order to determine whether the findings specified below may properly be made, it shall set said application for public hearing; and a public hearing shall be held in all cases where carriers by railroad are involved unless the Commission determines that a public hearing is not necessary in the public interest. If the Commission finds that, subject to such terms and conditions and such modifications as it shall find to be just and reasonable, the proposed transaction is within the scope of subparagraph (a) and will be consistent with the public interest, it shall enter an order approving and authorizing such transaction, upon the terms and conditions, and with the modications, so found to be just and reasonable: *Provided,* That if a carrier by railroad subject to this chapter, or any person which is controlled by such a carrier, or affiliated therewith within the meaning of paragraph (6), is an applicant in the case of any such proposed transaction involving a motor carrier, the Commission shall not enter such an order unless it finds that the transaction proposed will be consistent with the public interest and will enable such carrier to use service by motor vehicle to public advantage in its operations and will not unduly restrain competition.

(c) In passing upon any proposed transaction under the provisions of this paragraph (2), the Commission shall give weight to the following considerations, among others: (1)

the effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected.

(d) The Commission shall have authority in the case of a proposed transaction under this paragraph (2) involving a railroad or railroads, as a prerequisite to its approval of the proposed transaction, to require, upon equitable terms, the inclusion of another railroad or other railroads in the territory involved, upon petition by such railroad or railroads requesting such inclusion, and upon a finding that such inclusion is consistent with the public interest.

(e) No transaction which contemplates a guaranty or assumption of payment of dividends or of fixed charges, shall be approved by the Commission under this paragraph (2) except upon a specific finding by the Commisson that such guaranty or assumption is not inconsistent with the public interest. No transaction shall be approved under this paragraph (2) which will result in an increase of total fixed charges, except upon a specific finding by the Commission that such increase would not be contrary to public interest.

(f) As a condition of its approval, under this paragraph (2), of any transaction involving a carrier or carriers by railroad subject to the provisions of this chapter, the Commission shall require a fair and equitable arrangement to protect the interests of the railroad employees affected. In its order of approval the Commission shall include terms and conditions providing that during the period of four years from the effective date of such order

such transaction will not result in employees of the carrier or carriers by railroad affected by such order being in a worse position with respect to their employment, except that the protection afforded to any employee pursuant to this sentence shall not be required to continue for a longer period, following the effective date of such order, than the period during which such employee was in the employ of such carrier or carriers prior to the effective date of such order. Notwithstanding any other provisions of this chapter and chapters 8 and 12 of this title, an agreement pertaining to the protection of the interests of said employees may hereafter be entered into by any carrier or carriers by railroad and the duly authorized representative or representatives of its or their employees.

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CONTROL EFFECTED BY OTHER THAN PRESCRIBED METHODS

(4) It shall be unlawful for any person, except as provided in paragraph (2), to enter into any transaction within the scope of subparagraph (a) thereof, or to accomplish or effectuate, or to participate in accomplishing or effectuating, the control or management in a common interest of any two or more carriers, however such result is attained, whether directly or indirectly, by use of common directors, officers, or stockholders, a holding or investment company or companies, a voting trust or trusts, or in any other manner whatsoever. It shall be unlawful to continue to maintain control or management accomplished or effectuated after the enactment of this amendatory paragraph and in violation of its provisions. As used in this paragraph and paragraph (5), the words "control or management" shall be construed to include the power to exercise control or management.

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PLENARY NATURE OF AUTHORITY UNDER SECTION

(11) The authority conferred by this section shall be exclusive and plenary, and any carrier or corporation participating in or resulting from any transaction approved by the Commission thereunder, shall have full power (with the assent, in the case of a purchase and sale, a lease, a corporate consolidation, or a corporate merger, of a majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the shares entitled to vote of the capital stock of such corporation at a regular meeting of such stockholders, the notice of such meeting to include such purpose, or at a special meeting thereof called for such purpose) to carry such transaction into effect and to own and operate any properties and exercise any control or franchises acquired through said transaction without invoking any approval under State authority; and any carriers or other corporations, and their officers and employees and any other persons, participating in a transaction approved or authorized under the provisions of this section shall be and they are hereby relieved from the operation of the antitrust laws and of all other restraints, limitations, and prohibitions of law, Federal, State, or municipal, insofar as may be necessary to enable them to carry into effect the transaction so approved or provided for in accordance with the terms and conditions, if any, imposed by the Commission, and to hold, maintain, and operate any properties and exercise any control or franchises acquired through such transaction. Nothing in this section shall be construed to create or provide for the creation, directly or indirectly, of a Federal corporation, but any power granted by this section to any carrier or other corporation shall be deemed to be in addition to and in modication of its powers under its corporate charter or under the laws of any State.